

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

Rate and Service Changes to Implement )  
Functionally Equivalent Negotiated Service ) Docket No. MC2005-2  
Agreement with HSBC North America Holdings Inc. )

OFFICE OF THE CONSUMER ADVOCATE  
FURTHER COMMENTS ON THE HSBC NSA  
(April 27, 2005)

Presiding Officer's Ruling No. MC2005-2/1<sup>1</sup> established April 27, 2005, as the date for filing reply briefs. The Office of the Consumer Advocate (OCA) hereby submits further comments on the HSBC NSA based upon the response received to interrogatory OCA/USPS-1 in Docket No. R2005-1. These comments amplify a cautionary note expressed by OCA in its initial comments.<sup>2</sup>

OCA/USPS-1 (Docket No. R2005-1) asked the Postal Service to update the manual and electronic returns unit cost figures used by witness Dauer in her Appendix A of the instant proceeding. The Postal Service stated that it had not updated manual or electronic return cost figures for FY 2005 (Year 1 of the HSBC NSA), but that it had done so for FY 2006.

According to part c of the interrogatory response, "the USPS version Manual Letter Returns Unit Cost for the Test Year (FY 2006) is estimated at 48.4 cents." In Appendix A of witness Dauer's testimony, she estimates a cost of 60 cents in Year 2.

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<sup>1</sup> "Presiding Officer's Ruling Establishing Procedural Schedule," issued March 29, 2005.

According to part f of the interrogatory response, “the USPS version Electronic Letter Returns Unit Cost for the Test Year (FY 2006) is estimated at 31.0 cents.” In witness Dauer’s Docket No. MC2005-2 submission in Appendix A, she estimates a cost of 37 cents in Year 2.

Thus, it appears that both manual and electronic returns unit costs have declined since witness Crum performed his cost analysis for the Capital One NSA, Docket No. MC2002-2. Of course, cost changes are no surprise since the costing information witness Crum relied on were part of the Postal Service’s filing in Docket No. R2001-1 and are now 4 years out of date.

OCA has substituted the new manual and electronic returns unit cost figures provided in response to OCA/USPS-1 for those originally presented in witness Dauer’s Appendix A. The results are presented in Tables 1 through 4 attached to these comments. Substituting the new unit cost figures reduces the ACS savings that can be achieved by inducing HSBC to agree to electronic returns for its UAA mail in lieu of manual returns.

OCA has developed two alternative analyses showing the decrease in total USPS value resulting from the reduction in ACS savings. OCA has also calculated two new Commission-style stop loss caps based upon the change in total USPS value.

Table 1 presents the total USPS value when the new unit cost figures are applied in Year 1 (2005), and inflated by a factor of 4 percent for the subsequent two years—the

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<sup>2</sup> “Office of the Consumer Advocate Comments on the HSBC NSA,” filed one day late, on April 21, 2005, at 3 -4. Presiding Officer’s Ruling No. MC2005-2/2, “Placing Testimony into Evidence and Closing the Record,” issued April 25, 2002, permitted consideration of the late-filed Comments.

approach used by witness Dauer.<sup>3</sup> Applying the new cost figures in Year 1 makes sense, and presents a reasonable estimate of total USPS value since the HSBC NSA will likely be implemented late in FY 2005 or early FY 2006. Based upon application of the new cost figures beginning in Year 1, the total value of the HSBC NSA to the Postal Service declines from \$6,277,748, as presented by witness Dauer, to \$5,067,058, as shown in Table 1—a net reduction of approximately \$1.21 million. Moreover, as a consequence of applying the new cost figures, a new Commission-style stop loss cap should also be calculated. Table 2, prepared by OCA, shows a new stop loss cap of \$7,174,572, a reduction of approximately \$1.75 million from the stop loss cap of \$8,919,559 developed by witness Dauer.

Table 3 presents the total USPS value of the HSBC NSA when the new cost figures are applied in Year 2 (2006) and inflated for the subsequent and final year of the agreement. The total value of the HSBC NSA declines to \$5,369,402, for a net reduction of \$908,346. Similarly, the new stop loss cap would be reduced by approximately \$1.58 million to \$7,340,321, as shown in Table 4.

The Postal Service states in the Docket No. R2005-1 response that, “Because it only a subset of the figures used, no assumptions should be made regarding effects on the NSA as a whole.” [sic] OCA does not disagree with that policy. The updated cost figures have not yet been fully vetted and OCA intends to inquire further into the nature of the cost reductions. OCA believes that its new calculations do lend further support to

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<sup>3</sup> USPS-T-1 at 16.

its view that future NSAs reflect all of the operational and cost differences that have arisen since the baseline NSA was considered.

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**Table 1**  
**USPS Value for HSBC NSA Based Upon New Manual and**  
**Electronic Returns Unit Costs Effective Year 1 (2005)**

<b>HSBC North America Holdings Inc. Model</b>				
<b>Negotiated Service Agreement Appendix A, page 12</b>	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Total</b>
<b>ACS Savings</b>				
(1) Statement Mail	\$ -	\$ -	\$ -	\$ -
(2) Marketing Mail Letter	\$ 1,144,970	\$ 1,845,173	\$ 2,342,213	<b>\$ 5,332,357</b>
<b>Contribution from New Volume</b>				
(3) Statement Mail	\$ -	\$ -	\$ -	\$ -
(4) Marketing Mail Letter	\$ 1,214,459	\$ 1,488,633	\$ 1,458,016	<b>\$ 4,161,108</b>
<b>(5) Total Exposure</b>	\$ 656,340	\$ 964,968	\$ 1,172,146	<b>\$ 2,793,454</b>
<b>(6) Total Incremental Discounts</b>	\$ 411,268	\$ 592,994	\$ 628,691	<b>\$ 1,632,953</b>
<b>(7) Total USPS Value</b>	<b>\$ 1,291,821</b>	<b>\$ 1,775,846</b>	<b>\$ 1,999,391</b>	<b>\$ 5,067,058</b>

**Table 2**  
**Stop-Loss Cap with New Manual and Electronic Returns Unit Costs Effective Year 1 (2005)**

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total NSA</u>
<b>A. Effects of ACS (Savings Estimate)</b>				
<b>First-Class Mail Marketing Letters:</b>				
(1) Before Rates Avg. Cost	0.1350	0.1404	0.1460	
(2) Avg. Savings from Returns	0.0072	0.0075	0.0078	
(3) Avg. Savings (Cost) from Forwards	-	-	-	
(4) Total Avg. Savings from ACS	0.0072	0.0075	0.0078	
(5) After Rates Avg. Cost	0.1278	0.1329	0.1382	
(6) Before Rates Volume	196,842,621	298,877,229	363,314,190	
<b>(7) Net Contribution Gain from ACS (Savings)</b>	<b>1,424,355</b>	<b>2,249,185</b>	<b>2,843,466</b>	<b>6,517,006</b>
<b>B. Effects of Lost Contribution (Revenue Leakage)</b>				
(8) Before Rates First-Class Volume	679,863,892	817,284,750	919,784,128	
(9) Volume Threshold for Discounts	615,000,000	725,000,000	810,000,000	
(10) Before Rates Volume Eligible for Discounts	64,863,892	92,284,750	109,784,128	
(11) Average Discount on "Exposed" Volume	0.0220	0.0244	0.0259	
<b>(12) Total Discounts on Before Rates Volume (Leakage)</b>	<b>(1,424,355)</b>	<b>(2,249,185)</b>	<b>(2,843,466)</b>	<b>(6,517,006)</b>
<b>(13) Net Increase in Contribution (before rates volume)</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
(14) Savings from ACS at Break-Even Volume	6,517,006	/1		
(15) Pass-through Percentage	100%			
<b>(16) Stop-Loss Cap Amount</b>	<b>6,517,006</b>			
(17) Ratio of DFS "Competitive Cap" to PRC Cap	1.1009			
(18) Cap with "Competitive Adjustment"	7,174,572			

**Table 3**  
**USPS Value for HSBC NSA Based Upon New Manual and**  
**Electronic Returns Unit Costs Effective Year 2 (2006)**

<b>HSBC North America Holdings Inc. Model</b>					
<b>Negotiated Service Agreement</b>					
<b>Appendix A, page 12</b>		<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Total</b>
<b>ACS</b>					
<b>Savings</b>					
(1)	Statement Mail	\$ -	\$ -	\$ -	\$ -
(2)	Marketing Mail Letter	\$ 1,423,448	\$ 1,774,205	\$ 2,252,128	\$ 5,449,781
<b>Contribution from New Volume</b>					
(3)	Statement Mail	\$ -	\$ -	\$ -	\$ -
(4)	Marketing Mail Letter	\$ 1,190,845	\$ 1,590,856	\$ 1,564,327	\$ 4,346,028
<b>(5) Total Exposure</b>		\$ 656,340	\$ 964,968	\$ 1,172,146	\$ 2,793,454
<b>(6) Total Incremental Discounts</b>		\$ 411,268	\$ 592,994	\$ 628,691	\$ 1,632,953
<b>(7) Total USPS Value</b>		<b>\$ 1,546,685</b>	<b>\$ 1,807,100</b>	<b>\$ 2,015,617</b>	<b>\$ 5,369,402</b>

**Table 4**  
**Stop-Loss Cap with New Manual and Electronic Returns Unit Costs Effective Year 2 (2006)**

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total NSA</u>
<b>A. Effects of ACS (Savings Estimate)</b>				
<b>First-Class Mail Marketing Letters:</b>				
(1) Before Rates Avg. Cost	0.1382	0.1350	0.1404	
(2) Avg. Savings from Returns	0.0090	0.0072	0.0075	
(3) Avg. Savings (Cost) from Forwards	-	-	-	
(4) Total Avg. Savings from ACS	0.0090	0.0072	0.0075	
(5) After Rates Avg. Cost	0.1293	0.1278	0.1329	
(6) <b>Before Rates Volume</b>	196,842,621	298,877,229	363,314,190	
<b>(7) Net Contribution Gain from ACS (Savings)</b>	<b>1,770,784</b>	<b>2,162,678</b>	<b>2,734,102</b>	<b>6,667,564</b>
<b>B. Effects of Lost Contribution (Revenue Leakage)</b>				
(8) Before Rates First-Class Volume	679,863,892	817,284,750	919,784,128	
(9) Volume Threshold for Discounts	615,000,000	725,000,000	810,000,000	
(10) Before Rates Volume Eligible for Discounts	64,863,892	92,284,750	109,784,128	
(11) Average Discount on "Exposed" Volume	0.0273	0.0234	0.0249	
<b>(12) Total Discounts on Before Rates Volume (Leakage)</b>	<b>(1,770,784)</b>	<b>(2,162,678)</b>	<b>(2,734,102)</b>	<b>(6,667,564)</b>
<b>(13) Net Increase in Contribution (before rates volume)</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
(14) Savings from ACS at Break-Even Volume	6,667,564	/1		
(15) Pass-through Percentage	100%			
(16) <b>Stop-Loss Cap Amount</b>	<b>6,667,564</b>			
(17) Ratio of DFS "Competitive Cap" to PRC Cap	1.1009			
(18) Cap with "Competitive Adjustment"	7,340,321			