

POSTAL RATE COMMISSION

In the Matter of:)
)
RATE AND SERVICE CHANGES)
TO IMPLEMENT BASELINE) Docket No. MC2005-3
NEGOTIATED SERVICE)
AGREEMENT WITH BOOKSPAN)

Room 200
Postal Rate Commission
901 New York Avenue, N.W.
Washington, D.C.

Volume 4
Thursday, October 20, 2005

The above-entitled matter came on for hearing
pursuant to notice, at 10:23 a.m.

BEFORE:

HON. GEORGE A. OMAS, CHAIRMAN
HON. TONY HAMMOND, VICE-CHAIRMAN
HON. DAWN A. TISDALE, COMMISSIONER

APPEARANCES:

On behalf of the United States Postal Service:

SCOTT L. REITER, Esquire
United States Postal Service
Law Department
475 L'Enfant Plaza, S.W., Room 6506
Washington, D.C. 20260
(202) 268-2999

Heritage Reporting Corporation
(202) 628-4888

APPEARANCES: (cont'd.)

On behalf of the Office of the Consumer Advocate:

SHELLEY S. DREIFUSS, Esquire
Postal Rate Commission
Office of Consumer Advocate
1333 H Street, N.W.
Washington, D.C.
(202) 789-6837

On behalf of the Association for Postal Commerce
Mailing & Fulfillment Service Association and R.R.
Donnelley & Sons Company:

IAN D. VOLNER, Esquire
RITA L. BRICKMAN, Esquire
Venable, LLP
575 7th Street, N.W.
Washington, D.C. 20004
(202) 344-4800

C O N T E N T S

WITNESSES APPEARING:
MATTHIAS EPP

<u>WITNESSES:</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>	<u>VOIR DIRE</u>
Matthias Epp					
By Ms. Dreifuss	---	473	---	512	---
By Mr. Volner	---	---	507	---	---

<u>DOCUMENTS TRANSCRIBED INTO THE RECORD</u>	<u>PAGE</u>
None	

E X H I B I T S

<u>EXHIBITS AND/OR TESTIMONY</u>	<u>IDENTIFIED</u>	<u>RECEIVED</u>
None		

P R O C E E D I N G S

(10:23 a.m.)

1
2
3 CHAIRMAN OMAS: All right. We're back on
4 the record.

5 Ms. Dreifuss, would you proceed? We are now
6 in closed session.

7 Whereupon,

8 MATTHIAS EPP

9 having been previously duly sworn, was
10 recalled as a witness herein and was examined and
11 testified further as follows:

CROSS-EXAMINATION

12
13 BY MS. DREIFUSS:

14 Q Mr. Epp, could you turn to your response to
15 OCA Interrogatory T-2-11(b)? This was provided under
16 seal.

17 There are several figures on that sheet of
18 paper, but I was not comfortable in reproducing it and
19 handing it out into the audience so I'm just going to
20 read from this sheet as I need to.

21 In this answer, Bookspan very commendably
22 provided OCA a breakdown of marketing expenditures.
23 As I look at these figures it appears that direct mail
24 is by far the dominant marketing expense for Bookspan.
25 Is that correct?

1 A Yes, that's correct.

2 Q In fact, let me make sure I understand this
3 correctly. Direct mail in this table means postage
4 paid? Is that what the line Direct Mail means?

5 A Direct mail means where we use a direct mail
6 package to solicit new members for membership in the
7 club.

8 Q Right. And the figures that you're
9 providing on that line, are they only for postage or
10 other expenses included?

11 A It would include the total expense cost for
12 the direct mail campaign.

13 Q Including your print and production costs?

14 A Correct.

15 Q I see. Below that I see a line for
16 Enclosures. Those don't mean mail enclosures; they
17 mean some other kind of enclosure?

18 A Enclosures is a term that's used for two,
19 four, six-page inserts that are placed in other
20 companies' shipments for the purpose of acquiring new
21 members.

22 Q I see. So Bookspan sometimes will place its
23 own inserts or enclosures into some other company's
24 solicitation? Well, it may not be a solicitation
25 piece. Into some other company's mail piece?

1 A That's correct. It could be product
2 shipments. It could be mail pieces.

3 Q And then the line below that is Print.
4 Would that be, for example, advertising in a newspaper
5 or a magazine?

6 A The category Print includes placements in
7 newspapers. It includes on-page advertisements in
8 magazines.

9 Q Okay. Then we have a line for
10 Telemarketing. [REDACTED]

11 [REDACTED]

12 [REDACTED]

13 [REDACTED]

14 [REDACTED]

15 [REDACTED]

16 [REDACTED]

17 [REDACTED]

18 [REDACTED]

19 [REDACTED]

20 [REDACTED]

21 Q Okay. In 2004 though Bookspan did spend [REDACTED]
22 [REDACTED] on telemarketing. Is that less than the
23 amount that was budgeted for 2004?

24 A Yes, it is.

25 Q Do you know what the total amount was that

1 had been budgeted for 2004?

2 A I do not recall the exact amount.

3 Q How about just a rough guess of what was
4 originally budgeted?

5 MR. VOLNER: Rather than guess, Mr.
6 Chairman, we will see whether we can provide that
7 information under seal for the record if it exists
8 anymore.

9 CHAIRMAN OMAS: Thank you, Mr. Volner.

10 MS. DREIFUSS: Thank you.

11 BY MS. DREIFUSS:

12 Q Below that there's a line for Internet
13 Marketing. I think most of us probably know what that
14 might be.

15 Then finally the last type of marketing
16 expense is Alternative or Other Costs. What would
17 fall under that category?

18 A Campaigns in this category would, for
19 example, include direct response television
20 advertisements.

21 Q [REDACTED]
22 [REDACTED]
23 [REDACTED]
24 [REDACTED]
25 [REDACTED]

1 [REDACTED]
2 [REDACTED]
3 [REDACTED]
4 [REDACTED]
5 [REDACTED]
6 [REDACTED]
7 [REDACTED]
8 [REDACTED]
9 [REDACTED]
10 [REDACTED]
11 [REDACTED] budgeting process
12 [REDACTED]
13 [REDACTED]
14 [REDACTED]
15 [REDACTED]
16 [REDACTED]
17 [REDACTED]
18 [REDACTED]
19 [REDACTED] it is higher
20 [REDACTED]
21 [REDACTED]
22 [REDACTED]
23 [REDACTED]
24 [REDACTED]
25 [REDACTED]

1 [REDACTED]
2 [REDACTED]
3 [REDACTED]
4 [REDACTED]
5 [REDACTED]
6 [REDACTED]
7 [REDACTED]
8 [REDACTED]
9 [REDACTED]
10 [REDACTED]
11 [REDACTED]

12 Q Generally speaking, when we look at your
13 marketing totals for 2004, 2005 and 2006 we see them
14 drop off fairly significantly between 2004 and 2005.
15 These are total marketing expenditures. Then they
16 rise slightly in 2006.

17 Would you say your total marketing
18 expenditures basically reflected that new approach
19 that you just described a moment ago with respect to
20 direct mail?

21 A Yes. Absolutely. When you look at the
22 numbers you will see that they decline in every
23 channel. This was not a decision that was made
24 unilaterally in one channel. It was a decision to
25 reduce the spending overall.

1 When you go back to our budgeting process it
2 means that we started cutting those segments that were
3 unprofitable regardless of channel. It might have
4 affected some clubs more than others.

5 Q Okay. Now, for direct mail in 2006 you're
6 expecting to as budgeted spend [REDACTED] What
7 assumption goes into that with respect to whether or
8 not there will be a rate hike in 2006 and whether or
9 not Bookspan will have an NSA in 2006?

10 A When we prepared this budget in May of this
11 year we knew that there would be a rate increase, so
12 we included the rate increase or an assumption for
13 rate increase in our budgeting process. We did not
14 include the existence of an NSA into our assumptions.

15 Q Let me see if I can understand the
16 implications of that.

17 If the Commission were to recommend the NSA
18 that's before it and it could be put into place
19 sometime in 2006, does that mean that because you've
20 budgeted [REDACTED] for direct mail that you would
21 not be able to respond to NSA discounts in 2006 since
22 you had had a budget that did not reflect such
23 discounts in place?

24 A As I indicated in my testimony, our
25 budgeting process takes several months, but the actual

1 investment decisions are being made on a campaign-by-
2 campaign basis, which means every month as we plan new
3 campaigns we evaluate the spending versus the expected
4 profitability.

5 We have always and will continue to shift
6 money between channels based on change of assumptions,
7 so in the case here should the NSA be approved and
8 should we have an incentive to mail more this will
9 provide direct mail with a cost advantage versus other
10 channels, and that would be something that would flow
11 into our calculations as we plan those campaigns.

12 Q Let me ask you a hypothetical question.
13 We're looking at a budget figure for direct mail of
14 [REDACTED] in 2006, which is based on the assumption
15 that there will be a rate hike of 5.4 percent, but no
16 NSA discounts.

17 Let's take that budget, and let's divide it
18 into two parts. In two equal parts, so we're going to
19 be talking about [REDACTED] for each half of fiscal
20 year 2006, those budgeted amounts. Actually, before I
21 proceed with the hypothetical I should ask you
22 something.

23 When you budget [REDACTED] for 2006 do you
24 anticipate that those amounts, generally about half of
25 it will be spent in the first half of the year and

1 about half of it will be spent in the second half of
2 the year?

3 A No, we don't assume that.

4 Q Do you have a history of spending more in
5 the first half of the year or more in the second half
6 of the year?

7 A The spending is driven by seasonality, and
8 the seasonality really plays into our equations again
9 with respect to profitability, expected profitability.

10 Different clubs, different segments have
11 differences in response rates at different times of
12 the year. There might be things that work in the
13 back-to-school season. There are things that might
14 work in February. There are things that might work
15 better in April.

16 Q Let me just ask it. It is a hypothetical,
17 so I'll just ask you to make a hypothetical assumption
18 that we can take this budget of [REDACTED] and divide
19 it into two equal parts, [REDACTED] to be spent in
20 the first half of fiscal year 2006 and [REDACTED]
21 to be spent in the second half of 2006.

22 Now, the hypothetical is in the first half
23 of 2006 we'll still have the conditions that were
24 assumed in the budgeting process, a 5.4 percent rate
25 increase and no NSA. In the second half of 2006 we're

1 going to change this a little bit by saying there will
2 of course still be the rate hike, but now there will
3 be an NSA.

4 What do you expect would happen to the [REDACTED]
5 [REDACTED] that had been budgeted for direct mail under
6 those circumstances?

7 MR. VOLNER: Mr. Chairman, if Ms. Dreifuss
8 is trying to get a number I'm going to object to the
9 question because this is simply a variation of a
10 hypothetical upon a hypothetical which is based upon
11 an assumption. At least this time the assumption is
12 that there will be a rate increase, which is an
13 improvement.

14 If she is simply asking him how they will
15 react in the context of an NSA and a rate increase,
16 I'm perfectly happy to let him answer it.

17 CHAIRMAN OMAS: Is that what you're trying
18 to --

19 MS. DREIFUSS: I have to confess I'm not
20 sure of the distinction Mr. Volner was making, but I
21 think if Witness Epp could answer that second question
22 I believe that's the answer I'm looking for.

23 BY MS. DREIFUSS:

24 Q I'm not asking obviously for you to change
25 [REDACTED] and transform it into [REDACTED]

1 That would be a foolish expectation on my part.

2 I wanted to ask you generally. Well, I'll
3 ask you first a simple question. Would Bookspan tend
4 to spend more on direct mail in the second half of the
5 year? That is, would the [REDACTED] tend to be a
6 higher number with an NSA or a lower number with the
7 NSA?

8 A Let me first respond for the sake of
9 clarity. We have 35 book clubs, and we operate about
10 [REDACTED] campaigns, direct mail campaigns per year, so to
11 make a statement here or to try to come up with how
12 this would affect each and every single one of those
13 campaigns or even some of those campaigns is truly
14 hypothetical.

15 Now, to your second part of the question the
16 existence of an NSA would help direct mail compared to
17 the other channels. It would definitely not hurt.
18 That's what I point out in my testimony.

19 The relative performance or the relative
20 profitability of direct mail would be better with an
21 NSA. Therefore, we would have an incentive of
22 shifting money currently allocated to some of the
23 other channels into the direct mail channel and
24 thereby grow the direct mail channel.

25 Q Am I correct that there is in effect two

1 effects that stem from the NSA? One effect is that it
2 will get discounts on some of its mail. That's
3 correct, isn't it?

4 A That's correct.

5 Q The discounts would tend to push the Postal
6 expenditures somewhat lower, wouldn't it?

7 A They would not. The discounts apply only to
8 a volume over a certain threshold. The baseline or
9 everything under the threshold number is not affected
10 by the discount.

11 Q I see. So you're saying that the [REDACTED]
12 [REDACTED] that I was talking about before could only go
13 up, but you're not sure how much, with NSA discounts
14 in place?

15 A What I said is it would definitely help the
16 direct mail channel.

17 When you go back through our process of how
18 we plan a campaign, every time one other channel has a
19 cost advantage relative to the other channels it is
20 more likely to get the marketing dollars.

21 Q Are you able to share an expectation about
22 whether you might see a 25 percent increase in the
23 expenditure or a 50 percent increase? Do you have a
24 feel for that?

25 A That would be pure speculation simply

1 because postage is one component of the overall
2 equation as we calculate a return on marketing
3 investment. There are other components.

4 Q Okay. I want to turn to the issue of
5 strategic business mail inserts. You answered that
6 question under seal. It's your answer to OCA
7 Interrogatory No. T-2-10 to you. You did provide an
8 answer under seal.

9 We're actually in a confidential mode now
10 anyway. Some of it has been discussed openly before
11 and some only confidentially. This is a confidential
12 answer, but I guess we're in the confidential mode so
13 we'll just continue in that mode. Some of what I'm
14 going to ask you about though actually touches on
15 matters that Bookspan was willing to disclose
16 publicly.

17 In your answer --

18 MR. VOLNER: I'm sorry. I seem to have lost
19 the interrogatory that you're referring to.

20 MS. DREIFUSS: Yes. It's OCA/Bookspan-T-2-
21 10.

22 MR. VOLNER: Okay. Thank you.

23 MS. DREIFUSS: Sure.

24 BY MS. DREIFUSS:

25 Q Do you have it, Mr. Epp?

1 A I can't find it right now.

2 Q I didn't bring an extra copy.

3 MR. VOLNER: Mr. Chairman, just to simplify
4 things I will supply the witness with a copy.

5 CHAIRMAN OMAS: Thank you, Mr. Volner.

6 THE WITNESS: Oh, yes. That I have. I
7 thought there was more.

8 MR. VOLNER: No.

9 BY MS. DREIFUSS:

10 Q In this interrogatory OCA asked you to
11 explain the circumstances in which Bookspan
12 incorporates promotional material of a strategic
13 business partner and you explain that this material is
14 only included in letter size pieces and not in flat
15 size pieces.

16 Why is it that inserts would only be placed
17 in letters and not in flats? That is your strategic
18 business partners' inserts.

19 A There's a very simple reason for this. The
20 letter pieces come with an envelope that make it easy
21 to insert a third party piece into this.

22 The other flats are usually either stapled
23 or bound, and they make it very difficult in the
24 printing process to include a third party piece.

25 Q I see. In your answer to (a), the next to

1 the last sentence, you say that Bookspan began testing
2 inserts this year. By this year you mean in 2005? Is
3 that correct?

4 A That's correct.

5 Q About when in 2005 did you start testing
6 such strategic partner inserts?

7 A I believe in the summer of this year.

8 Q So prior to the summer of this year when
9 Bookspan sent out solicitations it did not include any
10 other advertising content apart from its own
11 advertising content? Is that correct?

12 A Solicitations for new members did not. Yes.

13 Q At the end of your answer to Part (a) you
14 say it appears that the purpose for including a
15 strategic business partner's inserts is to defray
16 costs. Is that correct?

17 A That is correct. As a mailer or as a
18 marketer I'd rather not include a third party piece in
19 my mailing because it typically has a negative impact
20 on response so if I can do, I do without.

21 The reason we tested into this was because
22 we saw some of the costs increasing, and we were
23 looking for a way to defray some of the cost without
24 affecting the response rate. The response rate is the
25 most important thing for us to come out of this

1 mailing.

2 Q The payments that a strategic business
3 partner makes to Bookspan, generally will that allow
4 more mail pieces to be sent?

5 A What it does do, it allows us to keep
6 certain campaigns on our schedule. What this means is
7 that in mailings that are in danger of not meeting the
8 profitability thresholds we might be able to keep them
9 on our market plans.

10 Q Without help in defraying expenses then
11 you're suggesting you might not do the campaign at
12 all, or it might look a little different than you
13 initially planned it?

14 A There are cases where that could happen,
15 yes.

16 Q So it could go either way?

17 A Yes. We've tested this, as I say here. You
18 test it because you're not sure what the impact on
19 your response rate is.

20 If the third party piece has a significant
21 impact on your response rate than you cannot afford to
22 do it, and we would not do it anymore.

23 Q I brought with me today some materials that
24 Bookspan provided to my office and to others. I'm
25 going to ask you a few questions about those.

1 What I have in front of me is a library
2 reference that Bookspan provided to the Commission and
3 what it consists of I don't know, probably only OCA
4 has looked at I think, but it's fun. I invite others
5 to look at it. This is a public disclosure I believe.
6 That's my recollection.

7 MR. VOLNER: Yes, it is. I don't have any
8 problem.

9 MS. DREIFUSS: If anybody cares to look at
10 it following cross-examination please feel free.

11 BY MS. DREIFUSS:

12 Q Just at random I picked up an advertising
13 piece. It seems to be advertising Doubleday book
14 club. That's what I see on the outside of the
15 envelope.

16 When I open it up what I find inside I find
17 a business reply card and a single sheet of paper,
18 looks like a letter encouraging the recipient to join
19 the club and then I find it looks like a catalog.
20 It's about 32 pages long. It's got pictures of books,
21 and a little description of their contents and prices
22 for them.

23 I wanted to ask you if the term *insert* is a
24 proper name to apply to the catalog, to this 32 page
25 thing that's been inserted in the envelope. Is this

1 an insert?

2 A No, it's not.

3 Q Well, what is this called?

4 A It's a catalog.

5 Q How can I distinguish between an insert and
6 a catalog?

7 A To the extent you're referring to a third-
8 party insert that would not be for Doubleday book
9 club.

10 Q Inserts would not be for Doubleday book
11 club. Earlier in the cross-examination you mentioned
12 a Doubleday insert. I think you said it was a four to
13 six page document. I don't remember exactly what it
14 was, something that was four to six pages in length
15 and you called that an insert.

16 Is a four to six page piece of advertising
17 material an insert?

18 A You're earlier question referred to
19 enclosures in our marketing plan and at that occasion
20 I said enclosures are inserts that we place into other
21 companies' shipments.

22 Q Right. I remember that part of our
23 discussion, but much earlier in the cross-examination
24 that took place right at the very beginning you used
25 the term insert and you were referring to a four to

1 six page piece of advertising material of Bookspan.
2 Do you ever use the term insert to describe things
3 that go into a solicitation envelope?

4 A No. We refer to these pieces that you have
5 as direct mail packages and their components.

6 Q Do individual components have specific
7 names?

8 A Yes, they do.

9 Q I showed you three different things. One
10 looked like a business reply card. What would you
11 call that?

12 A We call that the business reply card.

13 Q Well, that's a surprise. Then I saw some
14 kind of letter. What do you call that?

15 A We call that a letter.

16 Q What do you call the 32 page thing that
17 looked like I guess the catalog?

18 A The catalog.

19 Q All right. Are those things enclosed in an
20 envelope?

21 A Yes. The mailing piece that you showed me,
22 they come in an envelope.

23 Q Nevertheless you don't call them enclosures?

24 A No, we do not.

25 Q Are they inserted into an envelope?

1 A Operationally, yes.

2 Q But you don't call them inserts?

3 A No, we don't.

4 Q Bookspan coined a specific name for its
5 strategic business partners materials and that name is
6 insert?

7 MR. VOLNER: Mr. Chairman, I'm going to
8 object to the question. The witness can be asked as
9 to the business plans with respect to third-party
10 materials, but the witness is neither responsible for
11 having drafted nor did he have any part of the
12 drafting of the negotiated service agreement or the
13 VMCS provision which these questions go to.

14 If Ms. Dreifuss is unsatisfied with the
15 terminology she can deal with that directly, but not
16 through the witness.

17 CHAIRMAN OMAS: Continue, Ms. Dreifuss.

18 MS. DREIFUSS: Thank you, Mr. Chairman.

19 BY MS. DREIFUSS:

20 Q Mr. Epp, is the term insert used at Bookspan
21 to denote anything specific?

22 A The term insert is a very generic term that
23 is used. Yes.

24 Q When Bookspan uses it what does it mean by
25 insert?

1 A There's different uses of the term insert.
2 We have the term third-party insert which is an
3 advertisement or a flyer for a third-party that is
4 being inserted into one of our envelopes. That would
5 be one use of the term insert. The other term is when
6 we insert into other companies' shipments or mailings.
7 That's a piece that we also call insert as it is being
8 prepared.

9 When we prepare a direct mail piece that you
10 showed me we do not refer to any of those pieces as
11 inserts. It's a direct mail piece. It is being
12 developed by one creative staff and one job so to say
13 because you have to make sure that the envelope
14 matches what prospects see once they open the
15 envelope.

16 Q Actually, your explanation is very helpful
17 because it reminded me of how you used insert when we
18 first started the cross-examination. I think you did
19 use insert to refer to advertising material of
20 Bookspan's that was included in another company's mail
21 piece, and in that instance you mentioned that
22 sometimes the Bookspan insert may be several pages in
23 length. Is that correct?

24 A Yes. That's correct.

25 Q About how many pages do those inserts tend

1 to run?

2 A They're mostly driven by the weight
3 limitations that the other party has.

4 Q So if another party has an ounce or an ounce
5 and a half to spare then the insert could run for
6 several pages I would imagine couldn't it?

7 A It's unlikely because mostly the weight
8 limitations are very small. That's why most cases
9 it's a two page insert.

10 Q I noticed in Bookspan's promotional material
11 that I have here in this library reference, I asked my
12 secretary to weigh your promotional materials and I
13 find that some of these letters weigh 1.4 ounces, 1.6
14 ounces, here's another one that's 1.4 ounces. I won't
15 go through everything, but many of them weigh as
16 little as 1.4 ounces.

17 Here's one that's 1.2 ounces. That would
18 allow quite a lot of weight to be added to this
19 promotion and still not exceed the weight restriction
20 on standard mail letters wouldn't it?

21 A It would, but as I said earlier our goal is
22 not to include as many of those pieces as possible.
23 The goal of a direct mail campaign is to recruit new
24 members into the book clubs. We use the combination
25 of materials that works best.

1 In some clubs that is a relatively thin
2 catalog and maybe just a letter or an order card, in
3 other clubs it would require more pieces either
4 because the club has a deeper selection or because we
5 need to extend the offer better. Our goal is not to
6 include those as many third-party pieces as possible
7 because as I said earlier they tend to depress your
8 response rate.

9 Q It's conceivable, though, that at some
10 future time you could include just a single insert
11 from a strategic business partner that might weigh an
12 ounce or one and a half ounces and run several pages
13 isn't it?

14 A It's very unlikely because such a piece will
15 take away the attention of the focus of the prospect
16 from our book clubs. Again, our goal is to recruit
17 members into our clubs. If you include a heavy
18 advertisement for somebody else in there then as a
19 marketing person I probably would not achieve my
20 goals.

21 Q Generally speaking how do you determine what
22 the other companies, the strategic business partners'
23 share of postage should be in one of your promotions?

24 MR. VOLNER: Mr. Chairman, I will allow the
25 witness to answer, but I want to point out that she's

1 made an assumption that the arrangements are based on
2 a share of postage.

3 THE WITNESS: There is no share in the
4 postage.

5 BY MS. DREIFUSS:

6 Q Well, what is the business arrangement --

7 A The arrangements typically in the insert
8 world are priced on the per thousand pieces inserted.

9 Q Is weight a factor in the price?

10 A Typically there is a weight limit. It's
11 typically a quarter of an ounce.

12 Q If an insert were an ounce as opposed to a
13 quarter of an ounce would a strategic business partner
14 pay more than for simply a one quarter ounce insert?

15 A We would probably reject that piece. We
16 would reject it because it takes away from the
17 mailing.

18 Q If you allowed the piece -- well, let me ask
19 you this. All other things being pulled, does
20 Bookspan want to put several pages of catalog material
21 into the hands of a recipient as opposed to just a few
22 pages because there's more advertising content in
23 several pages of material than just a few pages?
24 Would that generally be true?

25 A Generally we use the best package we can

1 create. The best package can have more pages, can
2 have fewer pages again depending on the club. We look
3 at this in the terms of expected profitability.

4 Of course it costs more to produce a 32 page
5 catalog than to produce a 24 page catalog, so if you
6 get a lift in response and an associated lift in
7 profitability that covers the cost of producing a 32
8 page catalog then we might go with that catalog, if 24
9 pages do and are more profitable we would go with that
10 one. That's how we make our marketing decisions.

11 Q When Bookspan places inserts in other
12 companies' mail pieces do you tend to pay more for a
13 six page insert than a two page insert?

14 A Most companies that we place our inserts in
15 have limitations on weight. They tend to be somewhat
16 uniform, they also allow us to print in large enough
17 quantities to make the piece economical.

18 Q How large is your insert program with other
19 companies? How many pieces do you tend to send every
20 year in another company's mail pieces?

21 A I do not have that number ready.

22 Q Do you think it's [REDACTED]

23 A Probably.

24 Q You mentioned as I say at the beginning of
25 oral cross-examination --

1 MR. VOLNER: Before you go on I'm not sure
2 that I understood that last question. Were you
3 talking about dollars or number of pieces?

4 MS. DREIFUSS: You're right. Thank you for
5 the clarification.

6 BY MS. DREIFUSS:

7 Q I was talking about pieces, [REDACTED]
8 pieces. Did you understand my question to refer to
9 [REDACTED] of pieces?

10 A I understood it as pieces. Yes.

11 Q Okay. Thank you. So you were saying you
12 think it's at least [REDACTED] of pieces that Bookspan
13 inserts in other companies' mail pieces?

14 A Yes.

15 Q Again, at the beginning of oral cross-
16 examination you mentioned that sometimes Bookspan will
17 include an insert of four to six pages in another
18 company's mail piece. Does that sometimes occur?

19 A It could occur.

20 Q Do you have an idea how much six pages
21 weighs?

22 A I don't.

23 Q Do you think it's about that quarter ounce
24 that you were talking about before or do you think it
25 might be a little bit more?

1 A It might be a little bit more. I mean, I
2 mentioned this earlier. These are examples of
3 inserts. The vast majority of our insert are probably
4 two-sided.

5 Q Sometimes you do mail six pages of material.
6 Is that correct?

7 A If the space allows. Yes. Meaning the
8 third-party sets the parameters. It's not us going to
9 a third-party and saying we want to mail this, it's a
10 third-party setting out certain limitations and we
11 operate within those parameters.

12 Q In your experience would the companies that
13 insert Bookspan's advertising material tend to charge
14 Bookspan more for six pages of content than for just a
15 two-sided single sheet?

16 A Most companies have one rate per insert up
17 to the weight limit.

18 Q Do they sometimes have a second rate tier
19 for materials that exceed the weight limit?

20 A Very uncommon.

21 Q I also brought with me examples of inserts
22 that Bookspan apparently has been testing this year.
23 I think you said it started in the summer of 2005.
24 There seem to be inserts of three different companies.
25 The first one is an [REDACTED]. Have you seen

1 that insert before?

2 A I believe I have.

3 Q [REDACTED] Have you seen that one?

4 A I'm not sure. I don't see every insert that
5 goes into our pieces.

6 Q Okay. I also see here this is an [REDACTED]
7 I think. Have you seen that one?

8 A I do not recall seeing that.

9 Q Then I've got several here from [REDACTED]
10 Have you heard of the company [REDACTED]

11 A Yes, I have.

12 Q Do you know what they sell?

13 A Cosmetic products.

14 Q Right. That's the way it appears in these
15 inserts. Then I've got some more inserts here from a
16 company called [REDACTED]. Do you know what [REDACTED]
17 sells?

18 A I think I do. Yes.

19 Q What do they sell?

20 A Vitamins?

21 Q I'm not sure myself. It seems to be a skin
22 care product. Maybe it's vitamins. It's very tiny,
23 so I'm having trouble reading it.

24 MR. VOLNER: Mr. Chairman, as counsel to the
25 company in question I will assure you it's a skin

1 product if it matters.

2 MS. DREIFUSS: Okay.

3 CHAIRMAN OMAS: Thank you for that, Mr.
4 Volner.

5 MS. DREIFUSS: Actually, my days of needing
6 it I think are long gone. I'm out of the acne product
7 phase of my life.

8 BY MS. DREIFUSS:

9 Q Does an [REDACTED]
10 have any obvious relationship to a book club?

11 A We have relationships with those companies
12 that extend far beyond the insertion into a new member
13 piece. For example some of those companies have
14 rented our mailing lists for many years and as such we
15 consider them partners.

16 Q I see, but in terms of the product being
17 sold at least it's not obvious to me a vacuum cleaner
18 doesn't really seem to have anything to do with a book
19 club. Is that a fairly accurate reaction on my part
20 do you think?

21 A It might not seem like this on the surface,
22 but again we have relationships with those companies
23 and they have used our mailing lists for years, so
24 clearly they find the universe to be responsive
25 otherwise they would not be spending their advertising

1 dollars in going into the shipment.

2 Q Bookspan's plans to establish a more --
3 well, let me ask you first does Bookspan plan to
4 establish a more significant strategic business
5 partner insertion program based on the test you
6 conducted this year?

7 A It will depend on the results of the test.

8 Q Have you gotten the results yet?

9 A We have some.

10 Q Where are they pushing Bookspan? Are they
11 pushing them toward continuing with the program or
12 dropping it?

13 A Some of the test results seem to indicate
14 that we took a hit in response rate that was not
15 compensated by those pieces and we have some tests
16 where it seems to come out even, meaning the
17 additional revenue compensated for the drop in
18 response rate.

19 Q If further tests indicate that it's a
20 successful program, that is overall it's profitable,
21 do you think Bookspan would tend to do more of it in
22 future years?

23 A I think what we will continue to do is
24 testing it because consumer response and consumer
25 acceptance of those pieces might change over time and

1 the results show that it does change by club.

2 Q Higher profitability when you use inserts
3 would I assume cause Bookspan to tend to continue with
4 a program. Am I correct in that assumption?

5 MR. VOLNER: There's an assumption in the
6 question beyond the assumption which is the word
7 *profitability*. If the witness understands the
8 question I certainly will allow him to answer it.
9 Profitability of the insert program is the way I
10 understand the question. Is that correct?

11 MS. DREIFUSS: That is correct.

12 THE WITNESS: We look at the profitability
13 of the campaign and that's the important thing. If
14 the campaign projects profitably and would outperform
15 a test without the inserts then there's a chance that
16 it would be retested and potentially applied to future
17 mailings.

18 MS. DREIFUSS: I have no further questions,
19 Mr. Chairman.

20 I thank you very much, Mr. Epp.

21 CHAIRMAN OMAS: Thank you, Ms. Dreifuss.

22 Is there anyone else who wishes to cross-
23 examine the witness?

24 (No response.)

25 CHAIRMAN OMAS: Are there any questions from

1 the bench?

2 COMMISSIONER TISDALE: I have one question.
3 You provided some volume estimates regarding
4 Bookspan's expected responses to both the proposed
5 rate case and the discount structure proposed in the
6 NSA. Can you explain why Bookspan would seem to be
7 more sensitive to the price changes from the NSA than
8 to the price changes that are a consequence of the
9 rate case?

10 THE WITNESS: The projections that we put
11 forward for the existence of the NSA are a threshold
12 for us which means this is no automatic thing. When a
13 rate increase happens that's a hard factor that we can
14 incorporate into our budgeting process. The existence
15 of an NSA since it provides discounts only after a
16 certain threshold is for us a goal that we will try to
17 achieve.

18 There's no automatic mechanism. That means
19 just simply because it is in effect will our volume go
20 up to the levels that we have projected. It will
21 require a shifting of marketing resources and it will
22 require us to work hard to come up with ways to
23 achieve that volume.

24 COMMISSIONER TISDALE: I'm not sure I really
25 understand. From what I saw in your responses to POIR

1 No. 1 you were expecting about a two and a half
2 percent decrease in letter size volume with the rate
3 increase for the first year of the test year. Is that
4 right?

5 THE WITNESS: I just want to make sure that
6 I'm looking at the right information that you're
7 referring to. That's POIR No. 1?

8 COMMISSIONER TISDALE: Yes.

9 THE WITNESS: I'm sorry. I'm not sure I
10 still remember your question. If you wouldn't mind
11 repeating that?

12 COMMISSIONER TISDALE: It looks like your
13 projection with regard to the rate increase would be
14 about a 2.5 percent decrease in letter size volume.

15 THE WITNESS: Well, it would result into the
16 numbers that I have here. I'm not sure if that's 2.5
17 percent, but it's the numbers as I submitted them.

18 COMMISSIONER TISDALE: Okay, but also for
19 that same year in response to the expected NSA
20 discount which would be about 10 percent you expect an
21 increase in letter volume of nearly 13 percent.
22 That's even excluding the ones that would be shifted
23 from flats to letters. That appears to be a much more
24 sensitive reaction to the NSA discount than to the
25 rate increase or the projected rate increase.

1 I was just wondering why there seems to be
2 that type of difference between the reaction of
3 Bookspan to the NSA discount as opposed to the rate
4 increase?

5 THE WITNESS: That's why I was referring to
6 my earlier answer. This is not an automatic increase
7 in mail volume. If the NSA were in existence we would
8 have to review our mailing program and make sure that
9 we increase the mailing volume. This will not come
10 alone from some of the postal savings.

11 There are other things we would have to do
12 in testing, into converting flats to letters and
13 seeing how we can shift money from other channels in
14 order to achieve those goals. That's what I said
15 earlier. It's not simply because of the existence of
16 an NSA the mail volume will just appear.

17 COMMISSIONER TISDALE: Okay. Thank you.

18 CHAIRMAN OMAS: Mr. Hammond?

19 VICE CHAIRMAN HAMMOND: No.

20 CHAIRMAN OMAS: Okay. is there anyone else?

21 (No response.)

22 CHAIRMAN OMAS: Mr. Volner, that brings us
23 to you, and would you like to redirect or you need
24 some time with your witness?

25 MR. VOLNER: I would like a few minutes with

1 the witness, Mr. Chairman, if that's all right with
2 you?

3 CHAIRMAN OMAS: Time? How much? How many
4 minutes?

5 MR. VOLNER: Seven minutes?

6 CHAIRMAN OMAS: All right. Why don't we
7 make it 10.

8 MR. VOLNER: Thanks.

9 CHAIRMAN OMAS: Thank you.

10 MR. VOLNER: Thank you, Mr. Chairman.

11 CHAIRMAN OMAS: We'll come back in 10
12 minutes. Thank you.

13 (Whereupon, a short recess was taken.)

14 CHAIRMAN OMAS: Mr. Volner?

15 MR. VOLNER: Thank you, Mr. Chairman. We do
16 have a few questions on redirect.

17 REDIRECT EXAMINATION

18 BY MR. VOLNER:

19 Q I want to start first with you answered a
20 number of questions including some questions by
21 Commissioner Hammond about the volume projections and
22 the budget. I want to make sure that we understand
23 the way the budget is built. First in terms of time
24 when you began the 2006 budget that would have been in
25 May of 2005. Is that correct?

1 A Yes. That's correct.

2 Q You assumed a rate increase of approximately
3 5.4 percent in developing the 2006 budget then?

4 A That's correct.

5 Q Now, was that simply an arbitrary assumption
6 or were you supplied with some information that led
7 you to that assumption?

8 A When we started the budgeting season the
9 media department that I'm responsible for reaches out
10 to different departments within Bookspan such as the
11 book production department, the editorial department,
12 the printing department to get estimates for paper
13 prices, book prices, postage rates, royalty rates for
14 the books that we ship out, et cetera.

15 All those assumptions flow into the
16 budgeting process.

17 Q Perfect. Now, the budget itself when you
18 develop it and bring it to closure I think you said in
19 October of each year does the budget contain a
20 specific count of a number of pieces generally that
21 you're going to use for direct mail for marketing to
22 new customers, new members?

23 A No. The key metrics that we budget for are
24 the new members recruited into our book clubs and the
25 money necessary to acquire them.

1 Q So that it's across all of the media?

2 A That's across all media, and that's how we
3 roll up the different media channels. We look at the
4 member intake as we call it, these are the members
5 recruited, and the advertising dollars spent in order
6 to get that intake.

7 Q So that as the year unfolds you don't do a
8 specific count well, so far this year we've mailed [REDACTED]
9 [REDACTED] pieces and our budget is [REDACTED], or [REDACTED] or
10 [REDACTED]?

11 A No. That is not a match rate that we manage
12 against. We managed against the spending and the
13 members recruited.

14 Q So that in developing the volume forecasts
15 that are in your testimony and are in POIR No. 1 you
16 made some sort of a judgment about what sort of
17 volumes are likely to be produced out of the budget?

18 A That's correct. We took our budgeted
19 numbers in spending and intake and tried to derive a
20 number of mail pieces from that.

21 Q Of course you were aware of what you had
22 done historically?

23 A Yes.

24 Q Now, you said in response to a question that
25 what the NSA does for you is it gives you an incentive

1 to mail more and I think you said it was a reach or
2 that you were going to have to increase testing to
3 achieve the incentive. I want to make sure I
4 understand what you mean by *incentive*.

5 Will it mean adding new internal lists to
6 the portfolio? You said at one point that you do
7 approximately [REDACTED] campaigns or mailing campaigns a
8 year. Will there be more mailing campaigns?

9 A What it will do is it will make certain
10 lists that currently are not profitable appear --
11 well, they will now project profitable. This can mean
12 then that certain lists are being added to campaigns
13 or that full campaigns will be added to the schedule.

14 Q Does it also mean potentially that you will
15 mail deeper into an existing list because lists are
16 not uniformly profitable I assume?

17 A Well, we make our decision on a list basis
18 so what could happen is that a list that did not make
19 the cut-off in the no NSA scenario would now be
20 eligible to be included in the campaign because it
21 projects to be profitable.

22 Q Now, one other line in this budgeting area.
23 I think we've established now that your baseline
24 budget which was in preparation before this case was
25 filed assumed no NSA and a 5.4 or something in that

1 order of magnitude rate increase.

2 You were asked and declined quite properly
3 in my judgment to try to quantify an assumption of no
4 rate increase plus the NSA and you said that would
5 take weeks if not more to rebuild the whole budget.
6 Is that because of the fact that you're now moving
7 that much further away from your baseline budget that
8 you were working from to begin with?

9 A Yes. It's one thing on the baseline to take
10 the baseline and make an estimate if one variable
11 changes, but that scenario is very hypothetical
12 because you would now be changing two of the
13 assumptions that went into the budgeting process.

14 Q One other matter and I think we're done.
15 There was an extended conversation about inserts and
16 there may or may not have been some discussion about
17 pieces that you put in with some other mailer's mail
18 piece, that you had essentially rented space in their
19 mail piece. You indicated that those pieces might be
20 as much as four to six pages in some cases.

21 Would it differ depending upon what sort of
22 a mail piece you were renting space? I mean, if
23 you're putting a piece into a Cosmetique box you might
24 have a greater tolerance than if you were putting a
25 piece into a Valpak letter piece? Is that likely to

1 be one of the criteria that comes into play?

2 A Yes. They are different insert programs.
3 Some are parcel insert programs if you want and others
4 are envelope insert programs.

5 Q The maximum permitted weight is going to
6 depend upon the type of the insert program in which
7 you're putting your piece?

8 A That's correct.

9 MR. VOLNER: I have no further questions,
10 Mr. Chairman.

11 CHAIRMAN OMAS: Thank you, Mr. Volner.

12 Is there anyone else who wishes to cross-
13 examine the witness?

14 Ms. Dreifuss?

15 MS. DREIFUSS: Mr. Chairman, I do have two
16 questions on re-cross based on the redirect.

17 RE-CROSS-EXAMINATION

18 BY MS. DREIFUSS:

19 Q Mr. Epp, one of the reasons you are
20 reluctant to provide the presiding officer as per the
21 Presiding Officer's Information Request No. 1 volume
22 estimates based on an assumption of no rate hike, but
23 having an NSA is that you feel that they are
24 judgmental. Is that your main concern about that?
25 It's too judgmental an exercise?

1 A No. The main concern is that we prepared as
2 part of our budgeting process a baseline which assumed
3 that there would be a rate increase, but no NSA.
4 Taking that rate increase out of the equation and at
5 the same time putting into the equation the existence
6 of an NSA would mean that I would have to change two
7 of the variables in trying to estimate the mail
8 volume.

9 That is significantly more hypothetical if
10 you want if you just were to change one of the
11 variables.

12 Q In your testimony you did provide very
13 specific volume estimates for the years 2007 and 2008.
14 What was your assumption about whether there would be
15 any rate increases during that period of time or not?

16 A As I said in my testimony the forecast
17 includes a projected rate increase in 2006 and also
18 includes a further postage increase in 2007.

19 Q You assumed that there would be another rate
20 increase in 2007 on top of the 5.4 percent going into
21 affect in 2006?

22 A Yes. That's what I said in the testimony.

23 Q How large a rate increase did you assume
24 we'd be facing in 2007?

25 A We did not have precise information, so we

1 assumed a rate increase.

2 Q Well, you must have had some number that you
3 were using. I mean, was it five percent, was it 10
4 percent? There must have been some number that went
5 into that assumption.

6 MR. VOLNER: Mr. Chairman, I'm going to
7 object to the question. We're engaging in guesswork.
8 He's answered the question. They did not have a
9 number and that is the answer.

10 CHAIRMAN OMAS: Please continue, Ms.
11 Dreifuss.

12 MS. DREIFUSS: Thank you, Mr. Chairman.

13 BY MS. DREIFUSS:

14 Q I still puzzled by that. We see real
15 figures on a piece of paper and I assume those figures
16 are different based on the assumption. Could you just
17 state in words what your assumption was concerning a
18 rate increase for 2007? What did you assume?

19 A The set of numbers that you see here are the
20 result of two different exercises. The 2006 numbers
21 came out of our budgeting process which involved many
22 people over many months. The following numbers for
23 2007 and 2008 are our best estimate that we had at
24 that time. So we assumed an increase in postal rates
25 for 2007.

1 We did not quantify this to a certain number
2 with the number of decimals behind that.

3 Q So there was no limit in how large the rate
4 increase might be? It was some kind of increase, but
5 no assumption at all about size, whether it was 100
6 percent, 50 percent, 10 percent? No assumption about
7 that?

8 A I'm not sure 100 percent rate rise would be
9 realistic. We probably assumed a similar increase in
10 postal increases for that year.

11 Q So you're able to use your judgment to
12 produce a volume estimate for 2007 based on a new
13 postage figure that results from an omnibus rate
14 increase. Are you not able to do that? In fact isn't
15 that what you did in your testimony?

16 A Well, what we do here in preparing those
17 estimates is that I ask different departments within
18 Bookspan what their best estimate is of certain
19 changes in postal rates as we prepare those estimates
20 and those are the things that would flow into those
21 estimates.

22 Q So for 2007 you develop a letter estimate of
23 75 million pieces based on your discussions with other
24 departments. Is that correct? Is that what you just
25 told me?

1 A Yes.

2 Q Your estimate for 2008 was based on your
3 discussion with other departments. Is that correct?

4 A Yes.

5 Q What did you assume about any rate increase
6 for 2008? Did you assume that there would be one or
7 there would not?

8 A No. We did not assume.

9 Q You didn't make an assumption or you assumed
10 there would be no rate increase?

11 CHAIRMAN OMAS: Would you please move on?
12 This is sufficiently belabored.

13 MS. DREIFUSS: Yes, Mr. Chairman. I will.

14 BY MS. DREIFUSS:

15 Q Mr. Volner asked you if an NSA would allow
16 you to mail deeper into an existing mail list and I
17 think you said that it would. Is that correct?

18 A The way a mailing list is defined is a list
19 of prospects for similar criteria. You can not
20 necessarily mail deeper into a list because the way a
21 direct mail campaign is planned is you plan it list by
22 list. What I did say is that certain lists that did
23 not meet the threshold requirement before might now
24 meet the threshold requirement.

25 Q Would you expect that one of the key

1 differences between a list that would be more likely
2 to be chosen for a campaign as opposed to one that was
3 less likely to be chosen was the expected response
4 rate of the two different lists?

5 A It's the expected possibility that would
6 make that the criteria that we measure against.

7 Q Different response rates would be an
8 important, a key factor in assessing profitability of
9 two different lists wouldn't it?

10 A Response rate is one factor, one of many.

11 Q Is it an important one?

12 A It's important.

13 MS. DREIFUSS: I have no further questions,
14 Mr. Chairman.

15 CHAIRMAN OMAS: Thank you.

16 MR. VOLNER: We have no further questions,
17 Mr. Chairman.

18 CHAIRMAN OMAS: Thank you.

19 Mr. Epp, that completes your testimony here
20 today, and we appreciate your appearance and your
21 contribution to our record. Again, we thank you and
22 you are now excused, but before we adjourn just for
23 the record and clarification I would like to make the
24 statement again that Witness Posch's testimony and
25 designated cross-examination has been entered into

1 evidence.

2 With that this concludes today's hearing.

3 This hearing is adjourned. Thank you.

4 (Witness excused.)

5 (Whereupon, at 11:36 a.m., the hearing in
6 the above-entitled matter was concluded.)

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REPORTER'S CERTIFICATE

1
2
3 DOCKET NO.: MC2005-3
4 CASE TITLE: Rate and Service Changes to Implement
Baseline Negotiated Service Agreement with Bookspan
5 HEARING DATE: 10/20/05
6 LOCATION: Washington, D.C.
7

8 I hereby certify that the proceedings and evidence are
9 contained fully and accurately on the tapes and notes
10 reported by me at the hearing in the above case before the
11 United States Postal Rate Commission.
12

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14 Date: 10/20/05

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