

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

POSTAL RATE AND FEE CHANGES, 2006

Docket No. R2006-1

RESPONSES OF GRAYHAIR SOFTWARE
WITNESS CAMERON BELLAMY TO INTERROGATORIES OF
UNITED STATES POSTAL SERVICE (USPS/GHS-T1 -3-14)
(October 2, 2006)

GrayHair Software hereby submits the responses of Cameron Bellamy to interrogatories USPS/GHS-T1-3-14, dated September 22, 2006. Each interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,

CAMERON BELLAMY
GRAYHAIR SOFTWARE

USPS/GHS-T1-3.

You claim that GHS would sustain significant harm if the Postal Service proposal for pricing Confirm service is adopted (GHS-T-1 at 2).

(a) If your claim is supported by any expectations of costs or losses for GrayHair Software, please identify and quantify each source while explaining how you develop your estimates.

(b) How do any of the significant sources of harm identified in response to part (a) compare in magnitude to GHS revenues?

(c) If you are unable to quantify your claim of significant harm, please describe in detail each qualitative form of significant harm you expect if the Postal Service pricing proposal for Confirm service is adopted.

RESPONSE TO USPS/GHS-T1-3.

(a) Directly, our costs for Confirm data would increase by at least 460%, as stated in GHS-T-1, p. 16. Indirectly, we fear a decline in Confirm volume that the USPS itself assumes is 10%. The USPS has not done any market studies before substantially changing the established pricing model, so there is risk of a greater market decline. To see this, construct a table of what a First-Class mailer would need to pay for scans, versus what a mailer in other classes would pay. Not surprisingly, it will be found that the mailer in other classes always seems to have to pay 500% of what the First-Class mailer pays. What might that price differential do to the percentage rate of usage of Confirm for other classes?

(b) They would have a significant effect on GrayHair, as it would with any small firm, certainly enough to slow the development of new products and cause a reorientation in business strategy.

(c) See the response to USPS/GHS-T1-2(a).

USPS/GHS-T1-4.

- (a) How much did GHS pay the Postal Service for Confirm service in GHS' last complete fiscal year?
- (b) If the OCA proposal for pricing Confirm service is implemented, please estimate how much GHS will pay the Postal Service for Confirm service in the first year under the new prices.
- (c) Please estimate how much GHS would pay if instead the Postal Service proposal is implemented.

RESPONSE TO USPS/GHS-T1-4.

- (a) \$40,000
- (b) \$80,000 or more
- (c) \$220,000 or more

USPS/GHS-T1-5.

You assert that the value of Confirm service is sufficient that GHS and other Platinum Confirm subscribers "will readily pay for increased fees for subscriptions" (GHS-T-1 at 3), and that "Confirm service is essential to mailers" (GHS-T-1 at 15).

- (a) Does this mean that Confirm service has a high value of service to GHS? Please explain fully.
- (b) Does this mean that Confirm service has a high value of service to other Platinum subscribers? Please explain fully.
- (c) Please explain how that value of service manifests itself in GHS' business model. In other words, how does your business model take advantage of what Confirm service provides to GHS?

RESPONSE TO USPS/GHS-T1-5.

- a) Confirm service from the USPS provides raw data. GHS adds value to this data by storing it, querying it, presenting it, and interfacing with client systems. GHS has worked with the Postal Service toward the goal of fixing errors and omissions in the data.

b) GHS cannot answer this. The value may differ.

c) GHS adds value to the raw USPS data, must do so to attract and retain its customers, and hopes to do more of this. It takes time and resources to build upon the base provided by the raw data.

USPS/GHS-T1-6.

You claim that “per-scan charges [] will limit the market” for Confirm service (GHS-T-1 at 3).

(a) Do you think that per-scan charges will discourage resellers from seeking out additional customers?

(b) Would the proposed ability to postpone the purchase of additional units until you have signed a new customer provide additional flexibility when expanding your business in the future? Please explain fully.

(c) Please confirm that it is possible that the flexibility discussed in part (b) could benefit other customers, whether reseller or direct user. If you do not confirm, please explain completely.

RESPONSE TO USPS/GHS-T1-6.

(a) Resellers and new subscribers will be inhibited. Any ROI targets will be harder to meet, and some applications will be foregone. Deployment would still occur but only when it is cost effective, and there would be an uneven pattern of deployment across industry by mail class.

Does it really still make sense in 2006 for the USPS to build barriers to full mail tracking (for all pieces in a mailing) for mailers desiring that, particularly in Standard mail with its long history of relatively high variability in number of days to delivery, when scan costs “approach zero” (GHS-T-1, p. 18) ?

(b) No, because under the current pricing structure, the issue does not arise.

(c) It could be seen as a benefit, or as a burden that is not there under the current pricing structure.

USPS/GHS-T1-7.

You express concern about offsetting the startup costs of going into the Confirm business (GHS-T-1 at 3-4).

- (a) How much were GHS' startup costs?
- (b) How much of the startup costs have been recovered to date?
- (c) Have you made a profit each year since your business began (after considering depreciation or other expense related to startup costs)? Please provide a full response for each year of operation.

RESPONSE TO USPS/GHS-T1-7.

(a) GHS considers this confidential and sensitive business information. As a private firm, GHS does not disclose this proprietary financial information to anyone, and will not voluntarily answer this question. Furthermore, knowing this information for one Platinum subscriber would not support any generalization on the part of any party, and cannot have any relevance to the proceedings.

(b) See (a) above.

(c) See (a) above. GHS will state for the record that for the first several years of its operation, no profit was made.

USPS/GHS-T1-8.

You recognize that the Postal Service market research for Confirm accurately predicted the existence of a resellers market, and that the Postal Service has created markets in the past (drop shipment being one example (GHS-T-1 at 5-6)).

(a) Is it your understanding that one purpose of the Postal Service proposal for Confirm service was to “prohibit resellers”? Please explain fully.

(b) Does the Postal Service Confirm proposal “arbitrarily intervene [to] prohibit resellers”? Please explain fully.

RESPONSE TO USPS/GHS-T1-8.

(a) We don’t know of any such purpose and in fact suggested to the contrary, that the USPS should not want to prohibit resellers because they play a role that is positive on the whole. Still, the USPS witness states in oral testimony that he did not see how to raise rates without “people moving out from the Postal Service into the resellers” (p. 4154). This does not constitute prohibiting resellers, but it may amount to a concern with inhibiting them.

(b) GHS testified as follows: “As long as the Postal Service does not arbitrarily intervene in the market to prohibit resellers, and allows them to compete along with firms developing in-house proprietary solutions, their presence is quite predictable.” (GHS-T-1, p. 6) It is clear that the testimony makes no claim that the proposal would prohibit resellers, and GHS hopes that nothing more needs to be said on that topic.

USPS/GHS-T1-9.

(a) How does GHS view the introduction of the 4-state barcode for Confirm service?

(b) Does it constitute an additional market opportunity? Please explain fully.

(c) Would GHS have preferred not to see its introduction? Please explain fully.

(d) Please explain your views of what the 4-state barcode may provide to Confirm customers, including GHS, and to the Postal Service.

RESPONSE TO USPS/GHS-T1-9.

(a) It represents an opportunity to expand Confirm services and to fix some of the limitations that arise from reliance on the PLANET Code with its relatively limited information carrying capacity.

(b) Not in itself, but as a means to that end. The USPS provides raw data which can lead to the development of new opportunities by the USPS or subscribers.

(c) GHS has been a proponent of the 4-state barcode since it was first brought up in industry/postal meetings, based on prior usage by other postal services.

(d) Mailers, Confirm subscribers, and USPS can all benefit from the additional digits available to carry information. The USPS and industry can introduce new value added services. In particular, the USPS can launch new services from which it can derive revenue while at the same time lowering its operations costs, such as OneCode ACS.

USPS/GHS-T1-10.

Please refer to your testimony on page 14, lines 7-21.

(a) Please explain the basis of your understanding that Confirm is a “service that has no purpose except in the context of a mailer having provided mail pieces to the Postal Service already, and being concerned with their delivery being as consistent and reliable as possible.”

(b) This quotation seemingly indicates that the value of Confirm service derives solely from its use as a tool to inform mailers about the consistency and reliability of delivery. Is this your intended meaning? If not, please explain fully.

RESPONSE TO USPS/GHS-T1-10.

(a) We meant that scans are derivative. No one would buy scans, and in fact no one could buy scans, without a mail piece having been mailed for some other reason. To make these transient events into a profit center and try to give them the pricing attributes of the primary product appears to take a special pricing perspective, not the perspective of engineering or of operations.

(b) GHS believes that documenting service performance by measuring the consistency and reliability of delivery in all mail classes is essential for the future health of the Postal Service. Some other benefits to both USPS and mailers from unshackled access to Confirm scan data are listed in the response to USPS/GHS-T1-2(a).

USPS/GHS-T1-11.

You state on page 16 of your testimony that GHS expects to receive more than one billion scans during 2006.

(a) How many scans has GHS received so far in 2006 (or as of a date you specify)?

(b) When does 2006 end for purposes of aggregating the billion scans?

(c) How many scans will GHS get in a 12-month period assuming;

i) the Postal Service proposal is implemented, or

ii) the OCA proposal is implemented?

RESPONSE TO USPS/GHS-T1-11.

(a) GHS considers this confidential and sensitive business information which in some form is already available to the Postal Service. Would the Postal Service be allowed to publish volume data for some or all of its customers? If not, then we should not be required to disclose that same confidential and sensitive

business information. If that is what is required for participation by private firms in rate cases, it will have a chilling effect on further involvement.

In any event, the estimate already voluntarily provided in the testimony shows that GHS will be subject to a 460% increase under the USPS proposal, and if that estimate is exceeded, the percentage of increase would go up from there, in accordance with the table submitted by the Postal Service.

(b) See (a) above.

(c) We are unable to answer this with precision, but clearly the Postal Service proposal, premised on a 10% reduction in volume, and with a five-to-one ratio for scan prices in different mail classes, introduced without market studies, raises important concerns.

USPS/GHS-T1-12.

In the paragraph beginning on line 16 of page 16 of your testimony, you claim that internet pricing “requires that there be at least one level of service with the unlimited option.”

(a) Can you cite to any authoritative sources that share your view?

(b) If so, please identify each source, and explain how it drives your conclusion about the necessity for an unlimited option.

(c) Why does the principle of “internet pricing” apply to Confirm service? Please explain fully.

RESPONSE TO USPS/GHS-T1-12.

(a-c) We can cite the USPS testimony from MC2002-1 by a witness who was at that time the industry chair of the Mailers' Technical Advisory Committee:

...if Internet fees were assessed per mouse click, in many households a form of rationing would be practiced. On the other hand, with a monthly subscription fee, the users will consume more of the service. As with other parts of the information platform, such as electronic communication between the mailers and the Postal Service, the benefit to the Service is increased as the participation rates reach and surpass a critical mass. For example, if some mailers inform the Service of upcoming large mailing events, this allows for some degree of planning. But, if the largest mailers all gave advance notice of upcoming mailing events, then workload could be predicted, staffing adjusted, equipment utilization optimized, and productivity increased. Therefore, it only makes sense to encourage high participation rates through an attractive pricing policy. (MC2002-1, USPS-T-2, p. 6)

This viewpoint regarding Confirm was reinforced by Nick Barranca, USPS VP for Product Development. in his presentation on Confirm to the International Conference on Postal Automation (ICPA), held in Washington DC, on May 30 through June 2, 2006 (see p. 7):

...Confirm presented some novel and interesting policy concerns that needed to be addressed when pricing the product. Confirm was a service that would benefit not only postal customers, but also present the USPS with a novel view of its operations that may lead to important performance measurement benefits. While customer benefits begin to accrue at almost any level of usage, USPS greatest benefits were expected to flow from widespread usage of the product. This attribute, it was determined, justified a pricing stance that promoted product usage.

GHS believes that it is important that there be at least one option in which something of value is provided, with no transaction charge assessed, in order to lay the foundation for growth. As an Internet based example, Google could have chosen to charge a small fee initially for each search, but instead made available a capability that became widely used, and then set about to derive business revenue from those circumstances. Under

the OCA pricing proposal, USPS can continue to develop a capability that will be widely used, and will still cover its costs and make a contribution to institutional costs. This meets the rate case requirements while leaving future growth prospects unfettered.

USPS/GHS-T1-13.

Please refer to the paragraph on page 17, lines 8-13, of your testimony.

(a) Why do you believe that the Postal Service should ignore the fact that scans for which it imposes no direct or marginal charge are used to generate a substantial revenue stream for the recipient of those scans?

(b) In particular, why do you believe that the Postal Service should ignore that revenue stream when its own revenue for the service does not cover costs?

RESPONSE TO USPS/GHS-T1-13.

(a) GHS has not extensively studied the Postal Reorganization Act. But as we understand it, the Act lists nine criteria that should be considered in determining postal rate and fee levels. While the third of the nine criteria requires classes of mail to cover their costs, there is no criterion that directly pertains to the revenue stream of an individual firm or group of firms. It seems quite a stretch from the factors listed in the Act to the concept that the Postal Service might think of charging more or less profitable firms more or less for postage or services.

(b) The OCA pricing proposal for Confirm is intended to cover costs, and in fact proposes a contribution to institutional costs that slightly exceeds that proposed by the Postal Service itself.

USPS/GHS-T1-14.

Please refer to the paragraphs on page 17, lines 8-22, and your Conclusion on page 22 of your testimony.

(a) Please confirm that witness Mitchum presents the Postal Service proposal for Confirm service and accordingly represents the Postal Service in this proceeding. If you do not confirm, please explain completely.

(b) Please confirm that the “pricing department,” as you characterize it, represents the Postal Service in this proceeding, and not its own interests. If you do not confirm, please explain completely.

(c) On what legal or factual grounds do you base your opinion that the “pricing department” is making its independent proposals in this docket? Please be specific and respond fully.

RESPONSE TO USPS/GHS-T1-14.

(a) Confirmed.

(b) Confirmed.

(c) We have no direct knowledge of the specific activities that occurred as the Confirm pricing proposal took shape. We have made no claim that the pricing process is independent of the organization. Our concern is with the outcome of that process.