

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

RATE AND SERVICE CHANGES TO IMPLEMENT
FUNCTIONALLY EQUIVALENT NEGOTIATED
SERVICE AGREEMENT WITH BANK ONE
CORPORATION

Docket No. MC2004-3

ERRATA TO RESPONSE OF THE UNITED STATES POSTAL SERVICE
WITNESS PLUNKETT TO INTERROGATORY OF VALPAK DIRECT
MARKETING SYSTEMS, INC. AND VALPAK DEALERS' ASSOCIATION, INC.
(VP/USPS-T1-30)

The United States Postal Service hereby revises its response to the following interrogatory of Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. VP/USPS-T1-30, originally filed on August 16, 2004. Counsel for Valpak had asked for a clarification of the earlier response and the Postal Service agreed that the revision would be best accomplished through a filing of errata to the original response.

The interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,
UNITED STATES POSTAL SERVICE

By its attorneys:

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August 20, 2004

VP/USPS-T1-30.

The attached spreadsheets (Attachments 1-3) compare the returns that the Postal Service receives in 2005 (Year 1) (Attachment 1) and 2007 (Year 3) (Attachment 2) when Bank One Standard Mail converts to First-Class Mail. Column (1) of Attachments 1 and 2 shows the return for Standard Mail, column (2) shows the return from un-discounted First-Class Mail, and columns (3)-(8) compute the returns at the various discount levels contained in the NSA. For ease of comparison, the data in each column assume an incremental volume of 10,000,000 pieces.

a. Rows (2)-(8) of Attachments 1 and 2 compute the total contribution and the per piece contribution for each respective column. Please review the data in this part of Attachments 1 and 2 and confirm that the entries accurately reflect the assumptions made by the Postal Service in this docket as to price and unit cost. If you do not confirm, please indicate what changes should be made in order to conform with the assumptions made by the Postal Service in this docket.

b. Rows (9)-(23) of Attachments 1 and 2 compute the cost of handling returns of UAA mail for each respective column. Please review the data in this part of Attachments 1 and 2 and confirm that the entries accurately reflect the assumptions made by the Postal Service in this docket as to return rates (both manual and ACS), as well as the unit costs for manual and ACS returns. If you do not confirm, please indicate what changes should be made in order to conform with the assumptions made by the Postal Service and Bank One in this docket.

c. The unit costs of destruction on shown on row (20) of Attachments 1 and 2 are somewhat arbitrary entries. If you have a better estimate for the unit cost of destruction, please provide.

d. Rows (24)-(35) of Attachments 1 and 2 compute the cost of providing forwarding service and electronic ACS returns for each respective column. Please review the data in this part of Attachments 1 and 2 and confirm that the entries accurately reflect the assumptions as to forwarding rates and ACS returns, as well as the unit costs for forwarding and ACS returns, made by the Postal Service in this docket. If you do not confirm, please indicate what changes should be made in order to conform with the assumptions made by the Postal Service in this docket.

e. If you believe that any further adjustment(s) should be made with respect to the costs of forwarding and/or ACS returns for forwarded mail in Attachments 1 and 2, please explain clearly and fully the nature of each such adjustment, and indicate how it would affect (*i.e.*, increase of decrease) the costs shown in rows (34)-(35).

RESPONSE:

Before responding to the specific subparts of the question, it is important to emphasize that the assumptions made by the Postal Service concerning the

BANK ONE FCM vs STD Comparison for 2005		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	STD	FCM	FCM						
(1) (Discount)	(No discount)	(No discount)	\$0.0250	\$0.0300	\$0.0350	\$0.0400	\$0.0450	\$0.0500	
(2) Marketing Volume (millions)	10	10	10	10	10	10	10	10	10
(3) Price per Piece	\$0.177	\$0.292	\$0.267	\$0.262	\$0.257	\$0.252	\$0.247	\$0.242	
(4) Total Revenue (millions)	\$1.77	\$2.92	\$2.67	\$2.62	\$2.57	\$2.52	\$2.47	\$2.42	
(5) Cost per Piece including 1.23% return rate	\$0.087	\$0.107	\$0.107						
(6) Total Cost including 1.23% return rate (millions)	\$0.87	\$1.07	\$1.07	\$1.07	\$1.07	\$1.07	\$1.07	\$1.07	\$1.07
(7) Contribution Millions	\$0.900	\$1.850	\$1.600	\$1.550	\$1.500	\$1.450	\$1.400	\$1.350	
(8) Incremental Contribution per piece	\$0.090	\$0.185	\$0.160	\$0.155	\$0.150	\$0.145	\$0.140	\$0.135	
(9) Return Rate	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%
(10) Systemwide Return Rate	0.00%	1.23%	1.23%						
(11) Excess Return Rate	0.00%	7.77%	7.77%						
(12) UAA Volume (millions)	0.9	0.777	0.777	0.777	0.777	0.777	0.777	0.777	0.777
(13) Electronic Returns (millions)	0.000	0.000	0.660	0.660	0.660	0.660	0.660	0.660	0.660
(14) Manual Returns (millions)	0.000	0.777	0.117	0.117	0.117	0.117	0.117	0.117	0.117
(15) Electronic Return Cost per Piece	\$0.340	\$0.340	\$0.340	\$0.340	\$0.340	\$0.340	\$0.340	\$0.340	\$0.340
(16) Manual Return Cost per Piece	\$0.550	\$0.550	\$0.550	\$0.550	\$0.550	\$0.550	\$0.550	\$0.550	\$0.550
(17) Total electronic return cost (millions)	\$0.000	\$0.000	\$0.225	\$0.225	\$0.225	\$0.225	\$0.225	\$0.225	\$0.225
(18) Total manual return cost (millions)	\$0.000	\$0.427	\$0.064	\$0.064	\$0.064	\$0.064	\$0.064	\$0.064	\$0.064
(19) Total Return Cost	\$0.000	\$0.427	\$0.289	\$0.289	\$0.289	\$0.289	\$0.289	\$0.289	\$0.289
(20) Cost of Destruction per Piece	\$0.015	\$0.015							
(21) Total Cost of destruction (millions)	\$0.014	\$0.000	\$0.010	\$0.010	\$0.010	\$0.010	\$0.010	\$0.010	\$0.010
(22) Contribution after return cost adjustments (millions)	\$0.887	\$1.423	\$1.301	\$1.251	\$1.201	\$1.151	\$1.101	\$1.051	
(23) Incremental Contribution/pc after return cost adjustment	\$0.089	\$0.142	\$0.130	\$0.125	\$0.120	\$0.115	\$0.110	\$0.105	
(24) Assumed Forwarding Rate	0.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%
(25) Systemwide Forwarding Rate	0.00%	1.96%	1.96%	1.96%	1.96%	1.96%	1.96%	1.96%	1.96%
(26) Excess Forwarding Rate	0.00%	0.04%	0.04%	0.04%	0.04%	0.04%	0.04%	0.04%	0.04%
(27) Excess Forward pieces from conversion (millions)	0	0.004	0.004	0.004	0.004	0.004	0.004	0.004	0.004
(28) Cost per Forward, Year 1	\$0.345	\$0.345	\$0.345	\$0.345	\$0.345	\$0.345	\$0.345	\$0.345	\$0.345
(29) Total Excess Cost of Forwards, Year 1	\$0.000	\$0.001	\$0.001	\$0.001	\$0.001	\$0.001	\$0.001	\$0.001	\$0.001
(30) ACS Notices for forwarded mail (millions)	0	0	0.2	0.2	0.2	0.2	0.2	0.2	0.2
(31) Cost per ACS notice, Year 1	\$0.074	\$0.074	\$0.074	\$0.074	\$0.074	\$0.074	\$0.074	\$0.074	\$0.074
(33) Total Cost ACS notices for Forwarded Mail (millions)	\$0.000	\$0.000	\$0.015	\$0.015	\$0.015	\$0.015	\$0.015	\$0.015	\$0.015
(34) Contribution after forwards cost adjustment (millions)	\$0.887	\$1.421	\$1.285	\$1.235	\$1.185	\$1.135	\$1.085	\$1.035	
(35) Incremental Contribution/pc after return cost adjustment	\$0.0887	\$0.1421	\$0.1285	\$0.1235	\$0.1185	\$0.1135	\$0.1085	\$0.1035	
(36) Incremental Contribution of Standard Mail (millions)	\$0.887	\$0.887	\$0.887	\$0.887	\$0.887	\$0.887	\$0.887	\$0.887	\$0.887
(37) Contribution after Standard Mail conversion (millions)	\$0.000	\$0.535	\$0.399	\$0.349	\$0.299	\$0.249	\$0.199	\$0.149	
(38) Incremental Contribution/pc after Standard Mail adjust	\$0.000	\$0.053	\$0.040	\$0.035	\$0.030	\$0.025	\$0.020	\$0.015	

BANK ONE FCM vs STD Comparison for 2007		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	STD	FCM							
(1) (Discount)	(No discount)	(No discount)	\$0.0250	\$0.0300	\$0.0350	\$0.0400	\$0.0450	\$0.0500	
(2) Marketing Volume (millions)	10	10	10	10	10	10	10	10	10
(3) Price per Piece	\$0.177	\$0.292	\$0.267	\$0.262	\$0.257	\$0.252	\$0.247	\$0.242	\$0.242
(4) Total Revenue (millions)	\$1.77	\$2.92	\$2.67	\$2.62	\$2.57	\$2.52	\$2.47	\$2.42	\$2.42
(5) Cost per Piece including 1.23% return rate	\$0.094	\$0.116	\$0.116	\$0.116	\$0.116	\$0.116	\$0.116	\$0.116	\$0.116
(6) Total Cost including 1.23% return rate (millions)	\$0.94	\$1.16	\$1.16	\$1.16	\$1.16	\$1.16	\$1.16	\$1.16	\$1.16
(7) Contribution Millions	\$0.829	\$1.763	\$1.513	\$1.463	\$1.413	\$1.363	\$1.313	\$1.263	\$1.263
(8) Incremental Contribution per piece	\$0.083	\$0.176	\$0.151	\$0.146	\$0.141	\$0.136	\$0.131	\$0.126	\$0.126
(9) Return Rate	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%
(10) Systemwide Return Rate	0.00%	1.23%	1.23%	1.23%	1.23%	1.23%	1.23%	1.23%	1.23%
(11) Excess Return Rate	0.00%	7.77%	7.77%	7.77%	7.77%	7.77%	7.77%	7.77%	7.77%
(12) UAA Volume (millions)	0.9	0.777	0.777	0.777	0.777	0.777	0.777	0.777	0.777
(13) Electronic Returns (millions)	0.000	0.000	0.660	0.660	0.660	0.660	0.660	0.660	0.660
(14) Manual Returns (millions)	0.000	0.777	0.117	0.117	0.117	0.117	0.117	0.117	0.117
(15) Electronic Return Cost per Piece	\$0.000	\$0.368	\$0.368	\$0.368	\$0.368	\$0.368	\$0.368	\$0.368	\$0.368
(16) Manual Return Cost per Piece	\$0.000	\$0.595	\$0.595	\$0.595	\$0.595	\$0.595	\$0.595	\$0.595	\$0.595
(17) Total electronic return cost (millions)	\$0.000	\$0.000	\$0.243	\$0.243	\$0.243	\$0.243	\$0.243	\$0.243	\$0.243
(18) Total manual return cost (millions)	\$0.000	\$0.462	\$0.069	\$0.069	\$0.069	\$0.069	\$0.069	\$0.069	\$0.069
(19) Total Return Cost	\$0.000	\$0.462	\$0.312	\$0.312	\$0.312	\$0.312	\$0.312	\$0.312	\$0.312
(20) Cost of Destruction per Piece	\$0.016	\$0.016	\$0.016	\$0.016	\$0.016	\$0.016	\$0.016	\$0.016	\$0.016
(21) Total Cost of destruction (millions)	\$0.015	\$0.000	\$0.011	\$0.011	\$0.011	\$0.011	\$0.011	\$0.011	\$0.011
(22) Contribution after return cost adjustments (millions)	\$0.814	\$1.300	\$1.190	\$1.140	\$1.090	\$1.040	\$0.990	\$0.940	\$0.940
(23) Incremental Contribution/pc after return cost adjustment	\$0.081	\$0.130	\$0.119	\$0.114	\$0.109	\$0.104	\$0.099	\$0.094	\$0.094
(24) Assumed Forwarding Rate	0.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%
(25) Systemwide Forwarding Rate	0.00%	1.96%	1.96%	1.96%	1.96%	1.96%	1.96%	1.96%	1.96%
(26) Excess Forwarding Rate	0.00%	0.04%	0.04%	0.04%	0.04%	0.04%	0.04%	0.04%	0.04%
(27) Excess Forward pieces from conversion (millions)	0	0.004	0.004	0.004	0.004	0.004	0.004	0.004	0.004
(28) Cost per Forward, Year 1	\$0.374	\$0.374	\$0.374	\$0.374	\$0.374	\$0.374	\$0.374	\$0.374	\$0.374
(29) Total Excess Cost of Forwards, Year 1	\$0.000	\$0.001	\$0.001	\$0.001	\$0.001	\$0.001	\$0.001	\$0.001	\$0.001
(30) ACS Notices for forwarded mail (millions)	0	0	0.2	0.2	0.2	0.2	0.2	0.2	0.2
(31) Cost per ACS notice, Year 1	\$0.080	\$0.080	\$0.080	\$0.080	\$0.080	\$0.080	\$0.080	\$0.080	\$0.080
(33) Total Cost ACS notices for Forwarded Mail (millions)	\$0.000	\$0.000	\$0.016	\$0.016	\$0.016	\$0.016	\$0.016	\$0.016	\$0.016
(34) Contribution after forwards cost adjustment (millions)	\$0.814	\$1.299	\$1.172	\$1.122	\$1.072	\$1.022	\$0.972	\$0.922	\$0.922
(35) Incremental Contribution/pc after return cost adjustment	\$0.0814	\$0.1299	\$0.1172	\$0.1122	\$0.1072	\$0.1022	\$0.0972	\$0.0922	\$0.0922
(36) Incremental Contribution of Standard Mail (millions)	\$0.814	\$0.814	\$0.814	\$0.814	\$0.814	\$0.814	\$0.814	\$0.814	\$0.814
(37) Contribution after Standard Mail conversion (millions)	\$0.000	\$0.485	\$0.358	\$0.308	\$0.258	\$0.208	\$0.158	\$0.108	\$0.108
(38) Incremental Contribution/pc after Standard Mail adjust.	\$0.000	\$0.048	\$0.036	\$0.031	\$0.026	\$0.021	\$0.016	\$0.011	\$0.011

FOOTNOTES

Shaded footnotes indicate that the calculation for the Standard Mail column is different.

- (1) Price incentive level.
- (2) Marketing letter volume.
- (3) Revenue per piece from Appendix A page 3 at (9) less price incentive for First Class Mail; and page 8 at (3) for Standard Mail .
- (4) $(2) * (3)$
- (5) In Appendix A page 1 change return rates for marketing mail - Letters (4) to 1.23%. Cost from Appendix A page 4 at (18).
Standard Mail = page 9 at (21) * contingency.
- (6) $(2) * (5)$
- (7) $(4) - (6)$
- (8) $(7) / (2)$
- (9) Appendix A page 1 at (2)
- (10) Appendix A page 1 at (4)
- (11) $(9) - (11)$
- (12) $(11) * (2)$
- (13) $.85$ (ACS success rate) * (12)
- (14) $.15$ (ACS failure rate) * (12)
- (15) Appendix A page 1 at (7)
- (16) Appendix A page 1 at (9)
- (17) $(13) * (15)$
- (18) $(14) * (16)$
- (19) $(17) + (18)$
- (20) Place holder. I have no estimate for the cost of destruction however because the same procedures for FCM and Standard the cost is the same.
- (21) For FCM = $(13) * (20)$ and for Standard Mail = $(12) * (20)$
- (22) $(7) - (19) - (21)$
- (23) $(22) / (2)$
- (24) Unaudited Postal data from Capital One and expected for this customer.
- (25) MC2002-2, POIR-2, Q7. (Tr. 2/319.)
- (26) $(24) - (25)$
- (27) $(26) * (2)$
- (28) FCM forwarding costs from MC2002-2, POIR-2, Q7 $(.307 * 1.04^3)$ inflated to 2005, and $(.307 * 1.04^5)$ to 2007. For Standard Mail is destruction cost because no forwards, only destruction. (Tr. 2/320.)
- (29) $(27) * (28)$
- (30) $(2) * (24)$
- (31) ACS notices costs from MC2002-2, POIR-2, Q7 inflated by 4% for 3 years to 2005, and 5 years to 2007. (Tr. 2/320.)
- (33) $(30) * (31)$
- (34) $(22) - (29) - (33)$
- (35) $(33) / (2)$
- (36) Total Contribution of Standard marketing pieces
- (37) $(34) - (36)$
- (38) $(37) / (2)$

costs of providing returns and forwarding, and the net contribution less discount of mail qualifying for the NSA discounts, are highly conservative.

First, the Postal Service based its unit cost estimates for Standard Mail on the Postal Service's costing methodology, while using the Commission's methodology to estimate the unit costs of First Class Mail. (This situation arose because, perhaps relating to the settlement of Docket No. R2001-1, Commission versions of the inputs needed to construct a Standard Mail model were not available at sufficient levels of disaggregation, creating an obstacle most readily surmounted by using Postal Service version inputs for Standard Mail.) The Commission methodology tends to produce higher costs. Consistent use of the same methodology to estimate the mail processing and carrier costs for *both* Standard Mail and First-Class Mail would increase the net contribution less discount for each piece that migrated from Standard Mail to First-Class Mail. If the Commission's methodology were used to cost both mail classes, the estimated costs of Standard Mail (and the associated piggybacks) would increase, and the estimated contribution from Standard mail would decrease accordingly. If the Postal Service's methodology were used to cost both mail classes, the estimated costs of First-Class Mail (and the associated piggybacks) would decrease, and the estimated contribution from First-Class mail would increase accordingly. Either way, the estimated net contribution less discount for mail that migrated from Standard Mail to First-Class Mail would increase.

Second, my Appendix A includes a contingency allowance for First-Class Mail, but inadvertently omits one for Standard Mail. Unlike my Appendix A, the attached spreadsheet adopted the appropriate procedure of applying a contingency allowance to both First-Class Mail and Standard Mail. This correctly increases the net contribution less discount of pieces that migrated from Standard Mail to First-Class Mail as a result of the NSA discounts.

Third, the Postal Service's financial calculations in this case have assumed that all new First-Class mail volumes generated by the NSA discounts will be migrated volume – i.e., will be offset by a corresponding reduction in Standard Mail volume. If some organic growth in First-Class Mail volumes (i.e., non-migration volumes) also occur, net contribution less discount will be larger, for the obvious reason that such new First-Class Mail volumes will not entail any offsetting loss of Standard Mail contribution.

- a. If one assumes that the return rate in year 1 is 1.23 percent, then the unit cost of marketing letter mail is 10.0 cents (cell T27 in my Appendix A page 5). The attachment to this interrogatory assumes 10.7 cents, thus understating net contribution. Otherwise the calculations appear to be correct and are confirmed.
- b. Confirmed.
- c. I am not aware of any alternative estimates, though the \$0.015 is a reasonable assumption given that the cost of destroying UAA should be the same irrespective of mail class.
- d. Confirmed except for the following: If the assumed forwarding rate of Bank One's Standard Mail is zero, the cost of destroying the mail that would otherwise have been forwardable should be included.
- e. The estimated incremental contribution per piece after Standard Mail adjustment would be higher if the value of avoided forwarding costs could be calculated at this time. While an accurate estimate of this value is not currently available, I note that avoiding a single forward with a cost of \$0.345 would defray the cost of 4.5 ACS notices for forwarded mail.

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

Nan K. McKenzie

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August 20, 2004