

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

RATE AND SERVICES CHANGES TO IMPLEMENT
FUNCTIONALLY EQUIVALENT NEGOTIATED
SERVICE AGREEMENT WITH DISCOVER
FINANCIAL SERVICES, INC.

Docket No. MC2004-4

NOTICE OF UNITED STATES POSTAL SERVICE OF FILING ERRATUM TO
REQUEST OF THE UNITED STATES POSTAL SERVICE
FOR A RECOMMENDED DECISION ON CLASSIFICATIONS, RATES
AND FEES TO IMPLEMENT FUNCTIONALLY EQUIVALENT NEGOTIATED SERVICE
AGREEMENT WITH DISCOVER FINANCIAL SERVICES, INC. (ERRATUM)
(June 24, 2004)

The United States Postal Service hereby gives notice that it is today filing an erratum to the Request Of The United States Postal Service For A Recommended Decision On Classification, Rates And Fess To Implement Functionally Equivalent Negotiated Service Agreement With Discover Financial Services, Inc., which was originally filed on June 21, 2004. The request included a reference to "solicitation" on page four, which has been deleted.

The corrected Request follows.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.
Chief Counsel, Ratemaking

Brian M. Reimer
Attorney

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260-1134
(202) 268-3037; Fax -5402
June 24, 2004

Revised June 24, 2004

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

RATE AND SERVICES CHANGES TO IMPLEMENT
FUNCTIONALLY EQUIVALENT NEGOTIATED
SERVICE AGREEMENT WITH DISCOVER
FINANCIAL SERVICES, INC.

Docket No. MC2004-4

REQUEST OF THE UNITED STATES POSTAL SERVICE
FOR A RECOMMENDED DECISION ON CLASSIFICATIONS, RATES
AND FEES TO IMPLEMENT FUNCTIONALLY EQUIVALENT NEGOTIATED SERVICE
AGREEMENT WITH DISCOVER FINANCIAL SERVICES, INC.

Pursuant to chapter 36 of title 39, United States Code, the United States Postal Service has determined that it would be in the public interest, and in accordance with the policies and applicable criteria of that title, to implement the classifications, rates and fees contained in the attached Negotiated Service Agreement (NSA) with Discover Financial Services, Inc. (Discover or DFS). Accordingly, the Postal Service requests that the Postal Rate Commission submit to the Governors of the Postal Service a decision recommending the changes proposed in this filing.

When it issued its decision in Docket No. MC2002-2 recommending rate and fee changes necessary to implement the Capital One NSA, the Commission found

that it is consistent with the policies of the Act for the Postal Service and the Commission to explore new methods of improving postal service efficiency through new economically beneficial rate programs. See § 403(a). During the course of this proceeding both the Commission and the Postal Service have gained knowledge about how NSAs may impact the postal system and its users. Continuing this process should lead to a healthier, more flexible system of economically efficient rates.

PRC Op., MC2002-2, at 158 (¶ 8040).

Revised June 24, 2004

The Discover NSA, appended here as Attachment F, is a negotiated contract founded on the operational and service relationship between the Postal Service and Discover. It shares material terms and conditions with the baseline NSA with Capital One Services, Inc. (Capital One), considered by the Commission in Docket No. MC2002-2.¹ Attachment A to this Request contains proposed Domestic Mail Classification Schedule (DMCS) language implementing the Discover NSA, and Attachment B contains proposed Rate Schedule language.

The Commission's recently promulgated rules for consideration of NSAs properly separate so-called "baseline" NSAs from those that are "functionally equivalent" to baselines. PRC Order No. 1391 (February 11, 2004). Under these rules, review of functionally equivalent NSA proposals is expected to require substantially less time for Commission consideration than a baseline request. Id. at 48. In accordance with 39 C.F.R. § 3001.196, and for the reasons explained in the testimony and materials submitted with this filing, the Discover NSA follows this lead and is submitted as functionally equivalent to the baseline Capital One NSA.

It is worth noting that Discover is a direct competitor of Capital One, and, in pertinent respects, is similarly situated. See Direct Testimony Of Karin Giffney On Behalf Of Discover Financial Services, Inc. (DFS-T-1) at 2, 12-13.² Accordingly, Discover should have an opportunity to participate in a functionally equivalent NSA. As

¹ Pursuant to Postal Service Board of Governors Resolution No. 03-8, the rates, fees, and classifications recommended by the Commission in Docket No. MC2002-2 were formally implemented on September 5, 2003.

² The Postal Service has reviewed the testimony of Discover witness Karin Giffney and, in accordance with Rule 192 (b), 38 C.F.R. § 3001.192(b), states that such testimony may be relied upon in presentation of the Postal Service's direct case. See Direct Testimony Of Ali Ayub On Behalf Of United States Postal Service (USPS-T-1) at 1-2.

explained in the testimony supporting the instant request, it is especially important in cases such as this one, where a party to a proposed NSA is a direct competitor of a party to the baseline NSA, that the proceedings be expeditious. Ayub Testimony (USPS-T-1 at 19); Giffney Testimony (DFS-T-1 at 4).

Under the terms of the proposed NSA, the Postal Service, Discover, and other mail users are expected to benefit. In particular, the proposed rate and fee changes are expected to lead to a net reduction in the Postal Service's costs related to the handling of undeliverable-as-addressed mail. In addition, the Postal Service expects the changes to enable Discover to reduce its postage costs. If the volume conditions are met, the contribution to institutional costs required from all mail users will be reduced.

1. Functional Equivalence.

As noted above, the Postal Service submits that the Discover NSA is functionally equivalent to the current Capital One NSA. The Commission pointed out in Docket No. RM2003-5, Order 1391 at 50, that the analysis that determines whether an NSA is functionally equivalent to a baseline NSA involves a comparison of the literal terms and conditions of the NSAs, and a comparison of the effect that each NSA has on the Postal Service.

The comparison of literal terms and conditions focuses on whether each agreement rests on the same substantive functional elements. PRC Order 1391 at 50. As explained in the testimony of Postal Service witness Ayub (USPS-T-1) at 6-7, the Discover NSA is based on the same two key substantive functional elements that are central to the Capital One NSA and recommended changes -- an address correction element and a declining block element. As to the first element, if the DMCS is amended

as proposed, the Postal Service would provide to Discover, at certain levels of volume, electronic address corrections without fee for solicitations sent by First-Class Mail that are undeliverable-as-addressed and cannot be forwarded under existing regulations. See Attachment F (Discover NSA) at ¶¶ I.B and II.B-E. In return, Discover would agree to forgo requiring the Postal Service to return such undeliverable mail, under the existing service features of First-Class Mail. Id. at ¶ II.A. As to the second element, if the foregoing conditions are met, to encourage increased First-Class Mail volume, Discover would be eligible for per-piece discounts on those portions of its First-Class Mail volume that exceed specified volume thresholds. Attachment F at ¶¶ III.A and C. The Discover NSA also has a comparable effect on the Postal Service, including the provision of real ACS savings. Ayub Testimony (USPS-T-1) at 7.

The Compliance Statement (Attachment E to this request) contains a part-by-part analysis of differences between the functionally equivalent Discover NSA and the baseline Capital One NSA. These differences do not, in any way, detract from the functional equivalency of the two NSAs. To the contrary, the Commission and the Postal Service anticipated that there would be differences between baseline and functionally equivalent agreements even if they shared the same terms and conditions. Functionally equivalent agreements would likely include provisions that recognize the unique mailing characteristics of each company because of the differences in how individual companies conduct business, solicit customers, and make business decisions. See PRC Op., MC2002-2, at 31-40, 136-42. See also DMCS § 610.12; DMM G911.

To be comparable to the Capital One NSA, an agreement need not contain identical terms, such as the level of First-Class Mail volume. PRC Op., MC2002-2, at 141. A review of the Attachment E to this request reveals that while there are differences in wording between the Discover NSA and the Capital One NSA, the differences fall well within the parameters of DMM G911.

Accordingly, the Postal Service considers that it is appropriate for the Commission to review and recommend the operative rate and classification elements of the Discover NSA as functionally equivalent to the Capital One NSA, under the procedures specified in the Commissions' Rules of Practice and Procedure (39 C.F.R. § 3001.196).

2. Economic effects of the Discover NSA on the Postal Service.

The overall cost, volume, and revenue effects of the proposed Discover NSA are relatively modest, both in the first year of the proposed agreement and in later years. As proposed, the changes would apply to only one, discretely-positioned mailer. The duration of the rates, fees and classifications would be limited to three years by the terms of the NSA. The proposed changes would apply to the rates, fees and classifications for Address Correction Service and First-Class Mail. No other mail classes or special services would be affected.

The impacts of this proposal are described fully in the testimony of Postal Service witness Ali Ayub (USPS-T-1) at 10-14, Appendices A and B. The Postal Service estimates it will benefit by \$6.8 million over the life of the NSA -- \$8.0 million in ACS

Cost Savings plus \$2.0 million in increased contribution, minus \$3.2 million in revenues referred to in the Capital One proceedings as leakage.³

Witness Ayub also estimates that the Discover NSA will have minimal impact on Discover's competitors, the Postal Service's competitors, and on mail users. Ayub Testimony (USPS-T-1) at 14-15. In providing his analysis of the competitive impact, witness Ayub relies upon the extensive evidence in the Capital One case.⁴

It is worth noting that in its Opinion and Recommended Decision in the Capital One case, Docket No. MC2002-2, the Commission determined that the Capital One NSA's effect on competition was a minor concern, particularly since no participant alleged that the Capital One NSA would cause competitive harm. PRC Op., MC2002-2, at 79, 159. The Postal Service considers that the competitive impact of extending the same terms and conditions to Discover, a competitor of Capital One, should garner similar concern. The converse is not true, however. Failure to permit Discover, a similarly situated competitor, access to the functionally equivalent NSA could be seen as unduly or unreasonably discriminatory, in violation of the Postal Reorganization Act. See PRC Order 1391 at 52.

3. Other Matters

Attachment A to this Request includes the proposed addition of Domestic Mail Classification Schedule 611. Attachment B sets forth the proposed addition of Rate Schedule 611. To implement the Discover NSA, the Postal Service requests that the Commission recommend these additions. Among other provisions, DMCS 611

³ Witness Ayub refers to this amount as "discount exposure" in his testimony. Ayub Testimony (USPS-T-1) at 9, 10.

⁴ Particularly, Docket No. MC2002-2, Tr. 8/1571-1789 and Tr. 10/2060 to 2141.

prescribes the criteria for determining eligibility of Discover mail for the proposed rate changes, describes the conditions under which Address Correction Service fees would not be charged, describes the manner and conditions under which discounts would be applicable to Discover First-Class Mail volume, and specifies a duration of three years for the NSA. As explained in witness Ayub's testimony, USPS-T-1 at 17-19, the requested changes would conform to the criteria of 39 U.S.C. §§ 3622(b) and 3623(c).

The NSA provides a foundation for the changes to the DMCS and Rate Schedule, and those changes should be read in concert with the terms of the NSA. Among other provisions, the Discover NSA specifies: (1) the key conditions making the NSA possible; (2) obligations undertaken by Discover to ensure reduction of postal costs associated with handling of returned and forwarded mail; (3) volume thresholds pertaining to mail qualifying under the NSA for additional discounts; (4) information concerning other issues, such as monitoring, compliance, regulatory review, implementation, withdrawal, and cancellation; and (5) conditions affecting public communications, amendments, and notices.

Pursuant to the Commission's Rules of Practice and Procedure (particularly 39 C.F.R. §§ 3001.193 and 3001.196), the Postal Service is filing with this Request prepared direct evidence on which it proposes to rely. In recognition that the Discover NSA is submitted as functionally equivalent to the baseline Capital One NSA, this evidence consists of one piece of testimony, including appendices: the testimony of Postal Service witness Ali Ayub (USPS-T-1).

The rules for consideration of functionally equivalent NSAs provide opportunities for limitation of issues, and comparatively rapid resolution, compatible with participants'

sufficient exercise of their due process rights. The Postal Service has filed a Proposal For Limitation Of Issues that outlines its expectations regarding the issues present in this case. In Attachment E to this Request, the Postal Service has filed a listing of the Docket No. MC2002-2 testimony on which it intends to rely in this case. These filings are in accordance with the procedural framework for expeditious consideration of functionally equivalent NSAs embodied in the Commission's rules.

The page following this Request is an index of Attachments. The testimony has been marked for identification as shown in Attachment D. Further data submitted for informational purposes or in response to specific sections of the Rules of Practice are included in the other Attachments.

In accordance with the discussion, above, and the accompanying pleadings filed by the Postal Service and Discover today,⁵ other evidence on which the Postal Service intends to rely is being filed today by Discover. Evidence filed by the Postal Service is referenced in Attachment D to this Request.

The Postal Service considers that its submissions comply with the Commission's filing requirements in Rules 193 and 196 of the Rules of Practice and Procedure (39 C.F.R. §§ 3001.193 and 196). Should the Commission conclude otherwise, the Postal Service respectfully requests consideration of the conditional motion it has filed seeking a waiver of the pertinent filing requirements in those rules.

⁵ United States Postal Service Proposal For Limitation Of Issues; Request Of The United States Postal Service For Establishment Of Settlement Procedures; Statement Of The United States Postal Service Concerning Compliance With Filing Requirements And Conditional Motion For Waiver.

Finally, it should be noted that the proposed data collection plan (USPS-T-1, Appendix C) will provide the same types of data as the data collection plan approved in the Capital One case, Docket No. MC2002-2.

WHEREFORE, the Postal Service requests that the Commission submit a recommended decision in accordance with this Request.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.
Chief Counsel, Ratemaking

Brian M. Reimer
Nan McKenzie
Michael T. Tidwell

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260-1137
(202) 268-3012 Fax -5402
June 21, 2004

INDEX OF ATTACHMENTS TO REQUEST, MC2004-4
RATE AND SERVICES CHANGES TO IMPLEMENT FUNCTIONALLY EQUIVALENT
NEGOTIATED SERVICE AGREEMENT WITH DISCOVER FINANCIAL SERVICES, INC. (DFS)

- Attachment A: Domestic Mail Classification Schedule 611 Language
- Attachment B: Rate Schedule 611
- Attachment C: Certification
- Attachment D: Index of Testimonies, Exhibit Titles, and Associated Attorneys
- Attachment E: Compliance Statement
- Attachment F: Negotiated Service Agreement Between United States Postal Service and Discover Financial Services, Inc.

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.

Brian M. Reimer

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260-1137
(202) 268-3037; Fax -5402
June 24, 2004