

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

Rate and Service Changes to Implement)
Functionally Equivalent Negotiated Service) Docket No. MC2004-4
Agreement with Discover Financial)
Services, Inc.)

OFFICE OF THE CONSUMER ADVOCATE
REQUEST FOR A HEARING IN DOCKET NO. MC2004-4

At the prehearing conference in the instant proceeding, held on July 15, 2004, Postal Service counsel informed the Presiding Officer that the participants wished to take an additional week to determine whether it would be necessary to request a hearing. Tr. 1/11. During that period of time, the Office of the Consumer Advocate (OCA) continued to assess the evidentiary presentations of the Postal Service and Discover and determined that the Commission's and the public's interests would be best served by the filing of OCA testimony. OCA informed the Postal Service and Discover Financial Services, Inc. (Discover) of that intention.

The issues that concern the OCA at this point relate to the financial effect of the proposed NSA on the Postal Service. Thus, OCA has no problem with the Postal Service's motion to limit issues. However, in POR No. MC2004-4/1 at 2,¹ the Presiding Officer has requested more specific statements. Although discovery is not yet complete, the OCA has identified some issues that clearly warrant a hearing.

¹ "Presiding Officer's Ruling Establishing Procedural Schedule," July 20, 2004.

First, as in the baseline case, the Postal Service proposes to grant discounts to volume that would be mailed even in the absence of discounts. In the baseline case, this problem was eliminated by Capital One's revision of its before-rates volume estimates. Such a solution seems unlikely in this docket, since a recommended decision is likely to issue in fewer than 120 days, before any new volume information can materialize.

The chief issue that OCA will address in its testimony is whether a stop-loss cap can be calculated for Discover in the same way the Commission calculated a stop-loss cap for Capital One. OCA's preliminary calculations indicate that the proposed competitive cap of \$13 million is more than \$4 million dollars higher than a stop-loss cap calculated by the method recommended by the Commission in PRC Op. Docket No. MC2002-2.

OCA will also use discovery, and possibly oral cross-examination, to see whether the new costs incurred in moving Discover's mail from Standard Mail to First Class (First Class return costs and forwarding costs are of the greatest concern) are sufficiently outweighed by the additional contribution that the NSA is estimated to provide.

OCA notes that Discover witness Karin Giffney testifies that, "On a monthly basis, DFS procures over 40 mailing lists that make up the entire acquisition campaign mailing. We mail from these lists and *not from an internal prospect database.*" DFS-T-1 at 6 (emphasis added). Discover's address lists and mailing practices are not like Capital One's.

Under DMCS §610.2, Capital One is required to "update[] its databases within 2 days after receipt of address correction information in all future First-Class Mail

marketing campaigns.” By contrast, under proposed DMCS §611.2(b) in the instant proceeding, Discover is obligated to: “update[] any databases it uses for solicitation mail, other than First-Class Mail customer correspondence related to account holders, as specified by the Postal Service.” The Discover NSA establishes a far more generous requirement for Discover – Discover must update any of its solicitation mail databases 30 business days after receiving address correction notices from the Postal Service (NSA §II.B.).

But Discover does not have any internal prospect databases to update. It appears that future avoided returns and forwards of Discover’s First-Class solicitations mail cannot occur. If this is correct, then any mail Discover were to shift from Standard to First Class would generate new costs for returns and forwards without generating any savings. This is most troubling in the case of new forwards, as no attempt has been made to quantify the new costs.

It is also important to point out that in the baseline case, Capital One was incurring substantial physical return costs for its First-Class Mail *prior* to entering into the NSA agreement. One of the chief benefits of the NSA was to reduce high levels of return costs already being incurred. The Commission emphasized that:

The Postal Service estimates the ACS portion of the NSA will reduce its costs significantly. The savings are possible primarily because Capital One’s business plan utilizes First-Class Mail to send solicitations that are returned-to-sender at the rate of nearly one in ten. Tr. 2/38-39, 42. This exceptionally high return rate, applied to a large volume of First-Class solicitations, causes the Postal Service to incur significant costs in the course of physically returning UAA mail to Capital One.

PRC Op. Docket No. MC2002-2, para. 6006 (footnote omitted). By contrast, Discover’s Standard Mail solicitations currently do not include free return of its pieces; thus they

are not generating any return costs as Standard Mail. This contrast between the Discover NSA and the baseline NSA is significant.

Moreover, there is the prospect of new forwarding costs that arise from inducing Discover's Standard Mail solicitations to move into First Class. Capital One was found to mail an average of 5.6 First Class Mail solicitation pieces to each household in the United States, based on a total First-Class Mail solicitation volume of 768 million. See witness Crum's response to POIR 2, Q7, page 3 (Tr. 2/320), Docket No. MC2002-2. By contrast, Discover projects its after-rates First-Class Mail solicitation volumes at 174 million, 22.7 percent of Capital One's First-Class Mail solicitation volumes. This equates to an average of 1.27 pieces per household. Its repeat forwarding rate is small compared to Capital One's. Thus, witness Crum's methodology from the baseline case (POIR 2, Q7) will not work for the Discover NSA. OCA raises as an issue whether the 6.6 cents of additional cost for providing electronic Address Correction Notices to Discover (witness Crum's response to interrogatory NAA/USPS-T3-11 (Tr. 2/284), Docket No. MC2002-2) will be offset by the avoided forwards of Discover's much smaller (nearly non-existent) amount of repeated First-Class solicitation mailings to the same address.

In view of the issues identified above, OCA respectfully urges the Commission to proceed on the 120-day procedural schedule triggered by the need for a hearing.

Respectfully submitted,

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