

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

Rules Applicable to Baseline
And Functionally Equivalent
Negotiated Service Agreements

Docket No. RM2003-5

INITIAL COMMENTS OF THE UNITED STATES POSTAL SERVICE
(September 30, 2003)

On August 27, 2003, the Postal Rate Commission issued Order No. 1383, soliciting comments on proposed new rules to govern Commission proceedings relating to Negotiated Service Agreements. In addition to proposing minor conforming changes to Rules 5, 51, and 61, the Order proposed a new Subpart L (“Rules Applicable to Negotiated Service Agreements”), consisting of new Rules 190 through 198. (Proposed Rules 197 and 198, however, are simple shells, reserved for the later addition of provisions regarding subjects not covered substantively in the instant proposals.) As requested by Order No. 1383, the Postal Service hereby offers its initial comments on the proposed new rules.

Background

On June 2, 2003, the Governors adopted the Postal Rate Commission’s recommendation in favor of changes in rates and fees, based upon a Negotiated Service Agreement with a single mailer, Capital One (Capital One NSA). The Capital One NSA and the proceedings to consider the rate and fee changes necessary to

implement the NSA were groundbreaking. Speculation about whether the Postal Service would request and the Commission would recommend rates that apply to a single mailer, has now been supplanted by supposition about how best to build upon the success of the Capital One NSA.

The Capital One case itself mapped two of the next steps. First, it addressed how to expand the benefits of the Capital One NSA to other similarly situated mailers by adopting the approach set forth in a March 31, 2003 Stipulation and Agreement, which was signed by 13 participants in the proceeding. The Stipulation defined the terms of an NSA that are comparable to the Capital One NSA. Second, both the Postal Service and the Commission acknowledged the need for specialized rules of procedures tailored to the consideration of NSAs.¹

On August 27, 2003, the Commission instituted the promised rulemaking with its Order No. 1383, Notice and Order Establishing Rulemaking Docket for Consideration of Proposed Rules Applicable to Baseline and Functionally Equivalent Negotiated Service Agreements (NSA Rulemaking). As stated in the text of Order No. 1383 discussing its proposed rules, the Commission seeks to balance the development of an adequate

¹ Request of the United States Postal Service for a Recommended Decision on Experimental Changes to Implement Capital One NSA, at 5; Opinion and Recommended Decision on Experimental Rate and Service Changes To Implement Negotiated Service Agreement with Capital One, para. 8023; Decision of the Governors of the United States Postal Service on the Opinion and Recommended Decision of the Postal Rate Commission Recommending Experimental Rate and Service Changes to Implement Negotiated Service Agreement with Capital One at 2.

record against the burdens on the participants and itself, and to provide a timely review while protecting due process requirements.

The proposed rules clearly define NSAs. They recognize the unique procedural status of the mailer who enters into the NSA as a co-proponent of the requested rate and fee change. They acknowledge the difference in the review necessary for NSAs that are fundamentally derived from an agreement that has been previously recommended by the Commission, as opposed to new or unique NSAs that require *de novo* review. The rules limit an NSA's duration to three years, since estimates of future costs and volumes may become uncertain beyond that time, but they support extending an NSA if an updated analysis supports the renewal.

The Postal Service's comments on the rules address the following issues: the utility of some of the general requirement provisions regarding unavailability of information; the type of financial analysis that will be presented in multi-year agreements; the presentation of mailer-specific costs and elasticities, or suitable proxies; the impact analysis relating to parties outside of the NSA; the authority of the Commission to reject a filing; a recommended modification to Rule 195 to include a 150-day time limit for baseline NSAs; and the contents of the provisions currently labeled as relating to "functionally equivalent" NSAs. Also included, following the discussion of the above matters, is a section regarding relatively minor miscellaneous suggestions.

The primary goal of the Postal Service's comments is to ensure that its interpretation aligns with the Commission's expectations, and thereby avoids unnecessary conflicts during proceedings. A secondary goal is to elicit further guidance

on the amount of time the Commission anticipates a baseline NSA will take, an important issue when an NSA candidate assesses the likely transaction costs of pursuing an NSA. The Postal Service is hopeful that the rulemaking will facilitate the continued evolution of NSAs as one of the options for postal price-setting.

Proposed Rule 193

We begin with discussion of various paragraphs of Rule 193, the rule intended to govern contents of the request filings. With respect to the paragraphs discussed, the Postal Service identifies its concerns, and sets forth suggested changes.

Paragraph 193(a) General Requirements

Two subparts of Rule 193(a)(2) contain requirements that can safely be eliminated, together with their implicit invitations to litigate issues unrelated to the question of a proposed NSA's compliance with the Act. Rule 193(a)(2)(iii) contains a requirement for quantifying the cost of obtaining information required by the rules, but unavailable. The Postal Service's experience suggests that, given the provision of sufficient resources (*i.e.*, funding), contractors can at least attempt to develop currently unavailable information. This experience also indicates the possibility of paying a contractor to estimate the cost of having the contractor develop the needed information. By requiring the inclusion of cost estimates for obtaining unavailable information, however, the rule could be inviting participants to question the accuracy of any particular estimate. This could easily lead to a protracted dispute about what expense would be necessary to obtain suitable information, an issue outside the scope of those

relevant to responding to the Postal Service's request. If the Postal Service is unable to obtain required information, it can explain the circumstances surrounding the unavailability and the expense or effort required to obtain the information in its request or in a motion for waiver. The Commission already has legal tools available that permit it to address evidentiary shortcomings. Therefore, the Postal Service believes this new requirement is unnecessary and could lead to protracted and unneeded litigation of this issue that does nothing to advance the Commission's resolution of the real procedural and substantive issues raised by the request.

Rule 193(a)(2)(v) would require, for unavailable information required by the Rules, testimony on whether sufficiently reliable estimates were available, and if so, their specifics. This rule also holds potential for litigation of unnecessary issues. If the Postal Service provides the best available information in conjunction with a request, and if the Board of Governors authorizes its filing, then the Board has in effect arrived at a conclusion as to the sufficiency of the information provided. Further, should the Commission make a favorable recommendation, it would be founded on a conclusion that the information provided was a sufficient substitute. Since the Board and the Commission necessarily make, through their required actions, findings regarding the legal sufficiency of information provided, this rule serves no constructive purpose. The Postal Service's suggested restructuring of paragraph 193(a) is shown in the attachment to this pleading.

Paragraph 193(e) – Financial Analysis

Paragraph (e) of proposed Rule 193 sets forth the elements required for the financial analysis underlying each requested NSA. In general, the provisions of this paragraph appear to be intended to elicit a workable set of materials that should be sufficient to explain and justify the financial components of a proposed NSA. The Postal Service, however, has concerns about the structure of paragraph (e), and a few of its provisions. Some of these concerns cause the Postal Service to propose specific alternative language, which appears in the attachment to these comments. In other instances, the language of the paragraph seems satisfactory as proposed, but some additional discussion is warranted to ensure that our interpretation of that language will not conflict with what the Commission has in mind.

- *Multi-Year Agreements and the Test Year Concept*

As the text of Order No. 1383 makes plain, the Commission views a single-year “test year” analysis as inadequate for purposes of evaluating a proposed multi-year NSA. Order No. 1383, at 11. The Postal Service does not necessarily share this view. In most omnibus rate cases, there is the common expectation that any new rates established therein will likely remain in effect for significant periods of time beyond the test year. Yet this expectation has generally not triggered serious proposals to extend rate case financial analyses beyond the test year. Although there is always the possibility that shifting financial relationships in later periods would suggest varying potential rate consequences for different rate categories, usually no attempt is made to incorporate such possibilities into omnibus rate case recommendations. Limiting

financial analyses to a single test year period is simply one of many practical accommodations built into the ratemaking process to keep the exercise manageable. Since all other postal rates can be constructed on a test year basis, there is no overwhelmingly compelling reason to insist that NSA proposals be handled differently.²

At the same time, however, the Postal Service appreciates the Commission's interest in bringing to bear all information available and relevant to the evaluation of a proposed NSA. As indicated in Order No. 1383, an estimate which merely shows a multi-year NSA providing favorable financial results in the first year cannot necessarily be assumed to be proof of comparable favorable results over the entire duration of the agreement. Given the much more narrow set of potential changing circumstances over the multi-year period that could affect the financial results of the NSA (compared with the universe of potential changes that could affect aggregate postal finances in years beyond a test year), it makes sense to take reasonable steps to incorporate available information about such changes into the evaluation process. The logical approach to achieving this objective is to require the submission of relevant information within the filing, as contemplated by proposed paragraph (e).

In principal, therefore, the Postal Service has no objection to the requirement that some financial information be presented for every year of a proposed multi-year

² We note, for example, that the risks associated with a potentially material effect on the Postal Service's financial integrity associated with the outyears of an omnibus change in rates and fees are significantly larger than the corresponding risks associated with the outyears of an NSA limited to one mailer.

NSA. One potential weakness of paragraph (e) as proposed, however, is that it would appear to create the expectation that information from each year covered by the NSA would be equivalent in scope and reliability. As a practical matter, however, within the contexts of most NSA proposals, estimates from near years and far years are not created equal. In terms of postal forecasts, unless both near and far years happen to be periods for which full-blown rate case rollforward models have already been developed, the scope of the inputs available for construction of forecasts for the respective years will be markedly different.

In terms of mailer forecasts, the reality is likely to be even more stark. Experience in the Capital One case highlighted the difficulties faced by a mailer attempting to make a one-year forecast, when company-wide forecasts of that range are outside the realm of its normal business planning activities. Based on that experience, it seems reasonable to believe that, as a general proposition, attempting to advance the forecast horizon for individual mailer forecasts across multi-year periods would pose serious challenges. Moreover, at this point in time, no global solutions to those challenges are readily apparent.

The Postal Service is not advocating, however, that requirements pertaining to subsequent years from multi-year agreements be deleted from proposed paragraph (e). Instead, our proposal is that the paragraph be restructured to recognize what would seem to be a fairly immutable reality in multi-year deals of this type. As the deal is being developed among the parties, the most complete and comprehensive analysis is likely to be focused on the period for which the most tangible data are available – the

first year of the agreement. In contrast, thinking about subsequent years tends to be more tenuous, and projections are therefore usually going to be handled differently.³

The Postal Service proposes a restructuring of paragraph (e) to reflect these real world differences, by instituting separate requirements for the first-year financial analysis, and other requirements applicable to subsequent years. The proposed restructuring of paragraph (e) is illustrated in the alternative version of the proposed rules, attached to this pleading.

As shown in the attached version of paragraph (e) of Rule 193, the full panoply of requirements appearing in the paragraph as proposed by the Commission would continue to apply to the financial analysis for the first year of the NSA. (Obviously, at the time an NSA is proposed to the Commission, its actual start date is unknown, and therefore we refer to a “one-year period intended to be representative of the first year of the proposed agreement.”) Those requirements would appear in subparagraph (e)(1).

Subparagraph (e)(2) would relate to the financial analyses submitted for any subsequent years. It sets forth a three-step process to govern the financial analyses provided for such years. In essence, the approach suggested is to focus on identifiable changes from the first year, rather than proposing to build a separate analysis for each

³ The inherent tendencies of circumstances to change and uncertainty to increase over time, cited on page 3 of the Order in support of the proposed 3-year limit on NSA duration, necessarily translate into higher risks for multi-year agreements. The appropriate response, however, is not to ignore these tendencies, but to seek to ensure that the risks are appropriately shared amongst all interested parties. A more realistic approach to the forecasting process should aid in the achievement of that objective.

subsequent year from the ground up. Thus, the first step of the process would be to identify any factors that might cause the relevant elements of the financial analysis for a particular subsequent year to differ materially from the corresponding elements in the first year. Second, the potential effects of each factor identified would be examined, and quantified to the extent practicable. Third, the projected effects of all such factors would be aggregated into a restated financial analysis for each component of the agreement for that particular subsequent year.

The intent of the Postal Service's suggested restructuring of paragraph 193(e) is not to reduce the amount or the quality of the information that would be provided in response to this portion of the new rule. The intent, rather, is to more closely align the provisions of the rule with the process by which that information is actually likely to be developed – regardless of which version of paragraph (e) is ultimately adopted. In reality, there are quite often likely to be significant limitations on the amount and quality of information available for subsequent years, and a rule which makes that reality more transparent is preferred over a rule which might tend to mask it. The Postal Service agrees that everyone should be reviewing the potential financial impact for the duration of the agreement, but in the event that the terms of the agreement do not differ significantly over time, any perceived solace obtained from financial forecasts beyond the first year may, to some extent, be the product of false comfort.

Of course, when more comprehensive information happens to be available, the Postal Service would apply that information to the full extent possible. Thus, for example, if an NSA case were filed shortly after an omnibus rate case had been

initiated, and some or all of the subsequent years covered by the NSA fell within the range of years for which rate case forecasts were already provided, all relevant parts of that information would be incorporated into the analyses.⁴ Even in that situation, however, the ability of the NSA partner to forecast its own plans would likely not be materially enhanced merely by the availability of substantial rate case documentation pertaining to the Postal Service.

There is also one sense in which the Postal Service's suggested version of paragraph (e) could actually elicit more up-front information than the version proposed in Order No. 1383. The Postal Service's version, subparagraph (e)(2)(i), would require the identification and examination of any factor that "might" have a material effect on financial results in subsequent years. The result of this provision should be that matters of possible contention, in terms of whether or not there would be any material effect on the components of the deal, will be addressed in the filing, even if the postal analysts' conclusion is that any effect would not be material. In contrast, under the Commission's proposal, it is unclear why any issue would be discussed if it does not quantitatively affect the development of the required estimates. Consequently, an

⁴ It perhaps bears noting here, however, that in those instances in which a full-blown rollforward is *not* otherwise available, the Postal Service would not expect that the "cost level changes" referenced in our proposed subparagraph (e)(2) would need to be developed through the same elaborate process by which cost level factors are developed for inclusion in a rate case rollforward. Instead, what is contemplated is whatever type of analysis yields projections of cost level changes, suitable for the limited purposes of the NSA filing, that can be developed, explained, and documented with a reasonable amount of time and effort.

additional benefit of the Postal Service's suggested version of paragraph (e) is that, by putting the available information about such issues on the table earlier rather than later, it should reduce the amount of time likely to be necessary for litigation.

Thus, the Postal Service favors a restructuring of paragraph (e) of proposed Rule 193, as shown in the attachment. While this restructuring would still result in presentation of a financial analysis for each year of the agreement, the context within which the submitted analyses for subsequent years of the agreement should be evaluated would be much more clearly established. Obviously, however, the required up-front provision of this type of information with the filing necessarily represents a significant improvement relative to the situation experienced in the Capital One NSA proceeding.

- *Mailer-Specific Costs*

In addition to concerns about the forecasting difficulties presented by the "duration of the agreement" provisions of proposed paragraph (e), the Postal Service also has concerns about the "mailer-specific cost" provisions of that paragraph. The Postal Service, however, appreciates the Commission's desire to establish rules that "balance the development of an adequate record against the burdens on the participants and the Commission" (Order No. 1383, at 3), particularly in the area of the development of mailer-specific costs. Thus, while subparagraph (e)(5) of the proposed rule provides that the Postal Service develop mailer-specific information, including a discussion of "material variances between mailer-specific costs and system-wide average costs", the paragraph elsewhere states that if mailer-specific costs are not

available, the Postal Service is to provide a discussion of the suitability of the proposed costs as a proxy for mailer-specific costs.

Intuitively, there is some merit to the Commission's view that "using system average information is less likely to give a true representation of the financial effects of the agreement, especially in cases where the mailer's characteristics do not coincide with the system-wide averages." Order No. 1383, at 11. However, the Postal Service reiterates its position that determination of mailer-specific costs in all but the most extraordinary circumstances would be nigh impossible. Generally speaking, the Postal Service cannot hope to trace any particular customer's mail through the postal system, through facilities with differing mail mixes and resulting productivities, across different propensities to be processed on various types of equipment, and across legs of transportation between different origin/destination combinations with differing costs and utilization rates on the transportation legs.

As the Commission is well-aware, for many of the estimated cost avoidances underlying the development of rate category differences in omnibus and other rate cases, the Postal Service's cost analysts utilize a hybrid costing approach that relies on a combination of engineering cost models. The results of those models are tied back to the aggregate costs derived from the most disaggregated level of data from the cost systems underlying the CRA. The Postal Service cannot develop independent national estimates of unit costs for most rate categories of mail, even at the nationally-aggregated level. The engineering-based estimates associated with the individual rate categories are subsequently adjusted by CRA adjustment factors, such that the rate

category costs aggregate to the appropriate CRA aggregate. The development of mailer-specific costs would require another level of adjustment factors to tie to the rate category cost before a CRA adjustment factor was applied to move from the rate category level to the CRA category level. Such layering of adjustment factors could necessarily lead one to question the quality of the resulting estimate: was it the result of analysis, or of layers of adjustment factors?

As illustrated in the Postal Service's presentation of analysis in support of the Capital One Negotiated Service Agreement, the Postal Service can attempt to make changes to average costs when, as the Commission put it on page 11 of the Order, "a facet of the agreement is based on the mailer deviating from the averages," and the Postal Service is capable of measuring the difference. In the Capital One filing, the Postal Service utilized Capital One's First-Class Mail billing determinants to establish that the resulting average unit cost, before adjustment for the return ratio, was not unlike the average unit cost for First-Class Presort Mail as a whole. However, this analysis itself necessarily relied on the estimated average unit costs for the different rate category elements.

Fortunately, the Commission in proposed Rule 193(e) recognizes the difficulty of producing "mailer-specific costs" by providing that such costs be produced "when practical" and when so doing would not lead to an undue burden. In most cases, the Postal Service is likely to utilize nationally-aggregated data, adjusted for extraordinary and measurable differences associated with the mail of the particular Negotiated Service Agreement partner. A particular customer's various mail piece characteristics

might differ from the typical characteristics of other mail, but only those differences for which the effects on costs can be measured would be incorporated into the cost estimates. Consideration of other differences would be limited to the discussion of the suitability of proxy information.

In summary, with respect to mailer-specific costs, the Postal Service believes that the proposed language of paragraph (e) would provide it with the necessary latitude to structure its financial analyses, and allow it to avoid routine requests for waivers. The Postal Service wants to use the most accurate costs available, and has no intention of merely using subclass averages in circumstances in which we do not believe they do a good job of estimating the true costs of a specific mailer involved in a proposed NSA. We recognize that special studies may be appropriate in some instances. As the above discussion indicates, however, all concerned should be aware of the Postal Service's expectation that the availability of real mailer-specific cost information is much more likely to be the exception than the rule. As in the Capital One NSA case, however, this condition should not be an insurmountable impediment to the adoption of reasonably structured agreements.

Paragraph 193(f) Impact Analysis

The proposed rule also contemplates that the Postal Service shall include estimates of the impact of the NSA on competitors of parties to the NSA, including competitors of the Postal Service. Paragraph (f) of proposed Section 3001.193 (Contents of Formal Requests) reads:

(f) *Impact analysis.* Every formal request shall include an estimate of the impact over the duration of the Negotiated Service Agreement on:

- (1) competitors of the parties to the Negotiated Service Agreement other than the Postal Service;
- (2) competitors of the Postal Service; and
- (3) mail users.

The Postal Service shall include a copy of any completed special studies that were used to make such estimates. If special studies have not been performed, the Postal Service shall state this fact and explain the alternate bases of its estimates.

Order No. 1383, Attachment at 7.

The standard of analysis intended by this section is unclear. The use of the word “estimate” could imply some degree of quantitative analysis of competitive impact, rather than a qualitative assessment. However, the rule explicitly contemplates that the required analysis may be made without resort to special studies, provided some alternative basis is disclosed and explained. Moreover, the Commission states that the filing burden will vary depending on the characteristics of a particular NSA, with strictly cost-based NSAs requiring a reduced showing. Order No. 1383, at 13.

Although the Postal Service understands the impetus for the proposed provision, we are concerned that it could be interpreted to require an unduly burdensome and impractically high level of documentation. The Commission indicates that the intent of this section is to give the Commission a basis for analyzing issues raised by Professor John Panzar in Docket No. MC2002-2. Order No. 1383, at 12. However, it has been established that competitive concerns such as those raised by Professor Panzar cannot

be expected to apply to all NSAs. Among the factors giving rise to his concerns were the use of optional tariffs, and the sale of a monopolized input. The Commission recognized the possibility that not all NSAs give rise to competitive concerns when it distinguished strictly cost-based NSAs from others. *Id.* at 13. Perhaps some consideration should be given to limiting the applicability of requirement (f)(1) to specific types of NSAs.

Beyond the potential over-breadth of the proposed provision, compliance could present significant practical difficulties for the Postal Service depending on how the rule is interpreted and applied. For example, with respect to impact on competitors of NSA parties, even if it proves possible to define the relevant market and identify the relevant competitors, the Postal Service and the parties to the NSA are unlikely to have access to sufficiently detailed information regarding the cost structure, demand characteristics, financial assets, sales figures and marketing strategy of the relevant competitors to present quantitative estimates of the impact on such competitors, or on their demand for postal services. At best, the Postal Service and NSA parties can be expected to present a qualitative description of relevant economic considerations. To the extent that a more precise estimate of impact on NSA competitors is desirable, it seems likely that the entities best positioned to provide such information would be the competitors themselves. Such information could be provided during the course of the hearings on the NSA, and should not be expected to be filed at the onset of the case.

Similar considerations would apply to subsection (2), pertaining to impact on competitors of the Postal Service. The Postal Service lacks information regarding the

cost structure and other key financial data pertaining to its competitor's operations, and, in some cases, cannot even gain access to its competitors' unpublished or negotiated rate schedules. Under these circumstances, the Postal Service's ability to gauge the impact on its competitors of a given NSA is limited.⁵

The Postal Service does not believe that the Commission, in proposing this provision, intended that it become an oppressive requirement which could stifle potential use of NSAs. We thus encourage the Commission to clarify its expectation regarding this provision along the following lines: In each NSA filing, the Postal Service would be expected to present an analysis that demonstrates that the Postal Service considered the impact on competitors of the NSA parties and the Postal Service, and of mail users, and the basis for each analysis. (Either implicitly or explicitly, this analysis should provide some basis to conclude that the benefits of increased sales to the NSA partner at discounted rates would not be outweighed by lost revenue associated with reduced sales to the competitors of the NSA partner at what would have been full rates.) Once these threshold requirements, which may be satisfied by qualitative analyses, were met, the burden of demonstrating undue or excessive harm to

⁵ The Postal Service assumes that proposed subsection (2), which focuses on impact on Postal Service competitors, has been included to further the Commission's consideration of the effect of rate increases on "enterprises in the public sector of the economy engaged in the delivery of mail matter other than letters" pursuant to 39 U.S.C. § 3622(b)(4). The Postal Service expects that, in evaluating competition-related arguments under subsection (b)(4), the Commission will be concerned with protecting *competition*, not particular competitors. See *Direct Marketing Association v. United States Postal Service*, 778 F.2d 96, 106 (2nd Cir. 1985).

competitors would shift to those competitors. In this way, the filing requirement would spur appropriate consideration of competitive and mail user impact by the Postal Service prior to filing a case, but will not present such a formidable obstacle that NSAs will become impractically costly to the Postal Service and possible NSA participants.

In order to make more plain this intent, we also suggest that the wording of the provision be amended to remove references to “estimates” and instead refer to “analyses.” The amended provision would thus read:

(f) *Impact analysis.* Every formal request shall include an analysis of the impact over the duration of the Negotiated Service Agreement on:

- (1) competitors of the parties to the Negotiated Service Agreement other than the Postal Service;
- (2) competitors of the Postal Service; and
- (3) mail users.

The Postal Service shall include a copy of any completed special studies that were used to conduct such analyses. If special studies have not been performed, the Postal Service shall state this fact and explain the alternate bases of its analyses.

Paragraph 193(j) Rejection of Requests

Proposed Rule 193(j) would authorize the Commission to “reject any request under this subpart that patently fails to substantially comply with any requirements of this subpart.” This language duplicates provisions found in the general rules governing filings under 39 U.S.C. §§ 3622 and 3623. 39 C.F.R. §§ 3001.54(s), 3001.64(i). The Commission does not specifically comment on the proposal in its Notice, except to

observe that it parallels the same provision in Rule 54 and “require[s] no further explanation.” Order No. 1383, at 14.

The Postal Service must emphasize its long-held views that rejection by the Commission of a Postal Service request made under sections 3622 and 3623 of the PRA falls outside the bounds of the Commission’s lawful authority. The Postal Service’s position on this issue was comprehensively addressed in its commentary on the proposals that included identical language in Rules 54 and 64.⁶ We hereby incorporate and affirm that expression of the Postal Service’s position.

We acknowledge the Commission’s disagreement with the Postal Service’s position. Nevertheless, we must reiterate our concern that the proposed rejection rule could arguably provide the foundation for an evasion of the Commission’s responsibility to address and dispose of the substance of a proposal without adherence to the requirements of hearings and a recommended decision mandated by the statute. We also would categorically reject the argument that a purported rejection of a Postal Service request to consider proposed changes based on an NSA would affect the Postal Service’s authority to impose temporary rate and classification changes under 39 U.S.C. § 3641. In any event, we note that, in creating other specialized procedures in

⁶ Comments of the United States Postal Service In Response to Postal Rate Commission Notice of Proposed Rulemaking, Docket No. RM80-1 (March 12, 1980).

its rules, the Commission has refrained from incorporating similar provisions.⁷ The Postal Service recommends striking this language from the proposed amendments.

Proposed Rule 195

Proposed Rule 195 would govern procedures applicable to requests for a recommended decision on a baseline agreement. What is notably absent is any time limit for the proceeding, a feature found not only in proposed Rule 196, which would govern consideration of functionally equivalent NSAs, but in other specialized procedures as well.⁸

The Postal Service recommends a time limit of 150 days from the date of filing. Such a time limit would lower the perceived transaction costs, an important consideration for potential NSA candidates. During this time period, the Commission should be able to build an adequate record through a proceeding that is consistent with due process. In this regard, we note that the Commission routinely considers a wider range of issues that affect millions of mailers when deciding an omnibus rate case in ten months. A more limited inquiry into proposals that directly impact only one or perhaps several mailers should be manageable in five months.

⁷ 39 C.F.R. §§ 3001.57, *et seq.* (Market Response Rate Requests for Express Mail Service); 3001.67, *et seq.* (Requests Involving Experimental Changes); 3001.69, *et seq.* (Expedited Minor Classification Cases); 3001.161, *et seq.* (Rules for Expedited Review to Allow Market Tests of Proposed Mail Classification Changes); 3001.171, *et seq.* (Rules for Expedited Review of Requests for Provisional Service Changes of Limited Duration).

⁸ See Provisional Services, Rule 174; Experimental 67d; Market Test Rule 164, Expedited Minor Classifications, Rule 69c.

Subsequent proceedings of baseline NSAs will not require the lengthy consideration of all of the issues raised in the Capital One proceeding, which lasted almost eight months. In that case, the Commission needed to consider the Postal Service's request to consider the Capital One NSA under the Experimental Rules. The Commission also had to plow some challenging terrain in considering a variety of issues raised by participants' novel proposals. The proposed rules build on the Commission's conclusions regarding those issues. They will guide future filings, and should avoid the need to re-navigate through the same territory.

In particular, while the Capital One case had many issues unfold as the case progressed, such as those related to costing and competition, the proposed rules anticipate disclosures in the initial request. The Postal Service's recommendations for multi-year agreements, as proffered in these comments, should also increase the quality of the disclosure by identifying factors that might impact relevant operations, such as PARS, and their financial impact in the years subsequent to the first year of an agreement. By frontloading the disclosure and discussion of issues in the request, interested parties will be better able to assess their need for active intervention and to streamline their discovery requests. As such, a 150-day time limit is consistent with building an adequate record to meet the Commission's statutory duty.

Setting a time limit for requests to recommend Baseline NSAs will also lower the transaction costs for possible NSA partners, and encourage discussions leading to other NSAs. By failing to ascribe a time limit to baseline NSAs, when time limits are provided for every other special proceeding, the Commission appears to be implicitly

anticipating that NSA proceedings may well take the full ten months provided in the Postal Reorganization Act. Few mailers have the resources to pursue such a course. By adding a time limit to the rules governing baseline NSAs, the Commission would send an important signal to the mailing community that it anticipates that cases filed under its new rules can be reviewed fully within 150 days.

There are a number of other benefits to a time limit. The financial analysis will be predicated on the most recently available data. A proceeding limited to five months will be better aligned with the best available financial data than one that takes ten months to complete. Second, the Postal Service anticipates, as happened with Capital One, that a mailer may have to make a significant change to its operations to participate in the NSA. A shorter, more reliable time frame will help the mailer plan for its operational changes. Last, but not least, a shorter litigation period should allow the agreement to be implemented sooner than would a longer litigation period.

Proposed Rule 196

The proposed rules recognize the potential that an NSA may serve as a baseline for later agreements involving other mailers (see, e.g., proposed Rule 196). In this regard, they build on a footnote added to the proposed DMCS language by the Stipulation and Agreement filed in the Capital One proceedings. That footnote⁹ stated:

⁹ The Commission's Opinion and Recommended Decision and the Decision of the Governors in Docket No. Mc2002-2, as well as the most recent version of the DMCS made available on the Commission's website, fail to incorporate this language. In light of discussion about the footnote by the Commission and the Governors in their
(footnote continued...)

Comparable NSAs, involving adoption of electronic Address Correction Service in lieu of physical returns for First-Class Mail that qualifies for Standard Mail rates and declining block rates for First-Class Mail, may be entered into with other customers, as specified by the Postal Service, and implemented pursuant to proceedings under Chapter 36 of Title 39, of the United States Code.

This language also serves to define the minimum commonalities that other NSAs patterned after, or derived from, the Capital One NSA must share. Order No. 1383 refers to the Capital One NSA as the “baseline,” and any NSAs sharing the identified criteria as “functionally equivalent.” To avoid confusion that might be associated with a substantive characterization, the Postal Service proposes using the more neutral term, “derivative NSAs.”

The term “functionally equivalent” in DMCS terms arose in connection with the recently concluded Mailing Online experiment (Docket No. MC2000-2). There, functional equivalence was defined by four DMCS-specified operational characteristics of hybrid services that, upon certification by the Postal Service, could qualify them to enter mail pursuant to the Mailing Online classification language *without Commission proceedings under Chapter 36*. The footnote added to DMCS 610 (see previous footnote) refers to substantive components of a negotiated agreement, namely, 1) use of electronic Address Correction Service, in lieu of physical returns for First-Class Mail that could have been entered as Standard Mail, and 2) declining block rates. The

(...footnote continued)
respective decisions, and the fact that the Postal Service has already issued implementing regulations (see <http://www.usps.com/cpim/ftp/bulletin/2003/pb22104.pdf> at 21-23), the omissions appear to be oversights.

Commission recognizes, however, that additional information from an NSA might be needed before “functional equivalence” could be established. Order No. 1383, at 17, third full paragraph; see *also*, Order No. 1383, at 3, n. 3 (“benefit to the Postal Service” also available to help define “functional equivalence”).

In this light, the Postal Service believes that use of “functional equivalence” to describe derivative NSAs will cause unnecessary and unwarranted confusion. Unlike in the Mailing Online context, the characteristics of the proposed NSA might involve more than just equivalence of operational functions. The proponents will also know that the Commission will evaluate each proposal independently, in light of the facts described in the filing. Accordingly, the Postal Service suggests that use of the term “derivative NSAs” will, in practice, better describe the type of proposals that might be forthcoming, while avoiding any confusion that might stem from previous use of “functionally equivalent.” This document accordingly refers to “baseline NSAs” and “derivative NSAs.”

There is good reason to limit the proceedings needed to consider derivative NSAs, to the extent practicable. The expense and effort of participating in Commission proceedings can deter mailer initiatives. At a minimum, creation of a shorter, less complicated procedure for derivative NSAs should promote exploration and development of NSAs patterned after those that have already been favorably reviewed. In this light, the attempt in proposed Rule 196 to shorten the period required for the

Commission to consider derivative NSAs by foreclosing previously litigated issues from further litigation is viewed as essential.¹⁰

Order No. 1383 observes that the “general, functional, and operational aspects” of a derivative NSA will already have been litigated. Order 1383 at 16. Under either the Commission’s proposed version or the Postal Service’s suggested revision of Rule 196(a)(1), the Postal Service’s direct case in a request relating to a derivative NSA would necessarily address the similarities and differences between the derivative and the baseline NSAs. These facts should readily permit participants to identify any issues that are new and which they intend to contend. Accordingly, the Postal Service recommends a requirement that participants identify as issues the elements of the filing they intend to contest. The Postal Service accordingly suggests that a sentence be added to proposed Rule 196(b), as reflected in the Attachment: Any participant, not limited to those who appeared in a previous Docket, who intends to contend a particular issue in a derivative docket shall identify such issue(s) not later than 5 days before the pre-hearing conference.” This should permit the Commission to shape procedures to any contended issues at or shortly after the pre-hearing conference.

Miscellaneous Suggestions

Revised Rules 51 and 61: The last sentence of existing Rules 51 and 61 currently reads: “The Rules of General Applicability in *Subpart A of this part* are also

¹⁰ In the longer run, rules for derivative NSAs may, or may not, also prove workable when applied to renewals or modifications.

applicable to proceedings on requests subject to *this subpart*.” [Emphases added.] The proposed rules append a sentence to the end of Rules 51 and 61 that further refers to “Subpart L” and “this subpart”. The antecedent for the latter of these is somewhat ambiguous, notwithstanding that close parsing can lead to the correct answer. The ambiguity would be removed if “this subpart” in the additional sentence, were replaced, respectively, with “Subpart B” or “Subpart C”. The sentence in Rule 51 would accordingly read, “For requests of the Postal Service based on Negotiated Service Agreements, the Rules Applicable to Negotiated Service Agreements, Subpart L, supersede the otherwise applicable rules of Subpart B.”

Rule 196(b) would impose a hard copy service requirement on the Postal Service when filing a request for approval of a derivative NSA. As such, it returns Postal Service ratemaking to the hard copy world which the Commission has worked so successfully to leave behind. The Postal Service has no specific objection to this requirement as it may serve to increase the likelihood of actual service. However, the Commission could and should experiment with its website’s email notification capability to provide similar notice electronically. Email notification may ultimately prove itself sufficient to avoid the need for hard copy service.

Rule 193(a)(1), in the fifth line, needs “(s)” added so that it refers to “mail classification schedule(s).” The DMCS is organized into multiple schedules.

Rule 193(g) refers to “3001.193(f)(5),” when it appears the intended reference is “3001.193(e)(5).” In the attachment to these comments, not only is the paragraph reference changed from 193(f) to 193(e), which would appear to be necessary under

any version of the proposal, but the subparagraph has been changed to 193(e)(1)(ii) to conform with the restructured version of paragraph 193(e) being suggested by the Postal Service.

Rule 193(c) refers to “rate schedule” when it should refer to “rate or fee schedules.”

Conclusion

While important, the comments and suggestions discussed above regarding the Commission’s proposed NSA rules are, in the broader scheme of things, relatively modest. Overall, the Postal Service anticipates that the availability of a clear structure for most of the major elements driving the likely course of future NSA proceedings should enhance its ability to negotiate with prospective NSA partners. Obviously, we may still be in the relatively early stages of developing the full contours of what might be possible in terms of NSAs, and the premium on flexibility is likely to remain high as we

move forward. Nevertheless, the Postal Service would view the proposed rules, if modified in accordance with these comments, as a tangible step in the right direction.

Respectfully submitted,

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September 30, 2003

ALTERNATIVE RULE LANGUAGE SUGGESTED BY THE POSTAL SERVICE

For those portions of the proposed new rules for which the Postal Service is suggesting alternative language, as discussed in the text of these comments, the proposed alternative language is shown below. The suggested language would replace the corresponding language proposed in the attachment to Order No. 1383. Those portions of the proposed new rules for which the Postal Service is not proposing changes have been omitted, as no apparent purpose would be served by mere replication of those portions of the attachment to Order No. 1383.

Subpart B – Rules Applicable to Requests for Changes in Rates or Fees

Rule 51 Applicability

The rules in this subpart govern the procedure with regard to requests of the Postal Service pursuant to § 3622 of the Act that the Commission submit a recommended decision on changes in a rate or rates of postage or in a fee or fees for postal service if the Postal Service determines that such changes would be in the public interest and in accordance with the policies of the Act. The Rules of General Applicability in Subpart A of this part are also applicable to proceedings on requests subject to this subpart. For requests of the Postal Service based on Negotiated Service Agreements, the Rules Applicable to Negotiated Service Agreements, Subpart L, supersede the otherwise applicable rules of Subpart B.

Subpart C – Rules Applicable to Requests for Establishing or Changing the Mail Classification Schedule

Rule 61 Applicability

The rules in this subpart govern the procedure with regard to requests of the Postal Service pursuant to § 3623 of the Act that the Commission submit a recommended decision on establishing or changing the mail classification schedule. The Rules of General Applicability in Subpart A of this part are also applicable to proceedings on requests subject to this subpart. For requests of the Postal Service based on Negotiated Service Agreements, the Rules Applicable to Negotiated Service Agreements, Subpart L, supersede the otherwise applicable rules of Subpart C.

Rule 193 Content of Formal Requests

(a) General requirements.

- (1) Each formal request filed under this subpart shall include such information and data and such statements of reasons and bases as are necessary and appropriate fully to inform the Commission and the parties of the nature, scope, significance, and impact of the proposed changes or adjustments in rates, fees, and/or the mail classification schedule(s) associated with the Negotiated Service Agreement, and to show that the changes or adjustments are in the public interest and in accordance with the policies and the applicable criteria of the Act. To the extent information is available or can be made available without undue burden, each formal request shall include the information specified in paragraphs (b) through (k) of this section. If the required information is set forth in the Postal Service's prepared direct evidence, it shall be deemed to be part of the formal request without restatement.
- (2) If any information required by paragraphs (b) through (k) of this section is not available and cannot be made available without undue burden, the request shall include a request for waiver of that requirement supported by a statement explaining with particularity:
 - (i) The information which is not available or cannot be made available without undue burden;
 - (ii) The reason or reasons that each such item of information is not available and cannot be made available without undue burden; and
 - (iii) Whether it is contemplated that each such item of information will be supplied in the future and, if so, at what time.

(c) Rates and standards information. Every formal request shall include a description of the proposed rates, fees, and/or classification changes, including proposed changes, in legislative format, to the text of the Domestic Mail Classification Schedule and any associated rate or fee schedule(s).

(e) Financial analysis. Every formal request shall include an analysis, as described in paragraph (e)(1) of this section, of the effects of the Negotiated Service Agreement on

Postal Service volumes, costs and revenues in a one-year period intended to be representative of the first year of the proposed agreement. If the agreement is proposed to extend beyond one year, the request shall also include an analysis of the effects of the agreement on Postal Service volumes, costs and revenues in each subsequent year of the proposed agreement, as described in paragraph (e)(2) of this section. For each year, the analysis shall provide such detail that the analysis of each component of a Negotiated Service Agreement can be independently reviewed, and shall be prepared in sufficient detail to allow independent replication, including citation to all referenced material.

- (1) The financial analysis for the one-year period intended to be representative of the first year of the proposed agreement shall:
 - (i) set forth the estimated mailer-specific costs, volumes, and revenues of the Postal Service for that year, assuming the then effective postal rates and fees absent the implementation of the Negotiated Service Agreement;
 - (ii) set forth the estimated mailer-specific costs, volumes, and revenues of the Postal Service for that year which result from implementation of the Negotiated Service Agreement;
 - (iii) include a discussion of the effects of the Negotiated Service Agreement on contribution to the Postal Service for that year (including consideration of the effect on contribution from mailers who are not parties to the agreement);
 - (iv) utilize mailer-specific costs for that year, and provide the basis used to determine such costs, including a discussion of material variances between mailer-specific costs and system-wide average costs; and
 - (v) utilize mailer-specific volumes and elasticity factors for that year, and provide the bases used to determine such volumes and elasticity factors.

If mailer-specific costs or elasticity factors are not available, the bases of the costs or elasticity factors that are proposed shall be provided, including a discussion of the suitability of the proposed costs or elasticity factors as proxies for mailer-specific costs or elasticity factors.

- (2) The financial analysis for each subsequent year covered by the agreement (if the proposed duration of the agreement is

greater than one year) shall:

- (i) identify any factors known or expected to operate in that subsequent year which might have a material effect on the estimated costs, volumes, or revenues of the Postal Service, relative to those set forth in the financial analysis provided for the first year of the agreement in response to paragraph (e)(1) of this section. Such relevant factors might include (but are not limited to) cost level changes, anticipated changes in operations, changes arising from specific terms of the proposed agreement, or potential changes in the level or composition of mail volumes;
- (ii) discuss the likely impact in that subsequent year of each factor identified in paragraph (e)(2)(i), and quantify that impact to the maximum extent practical; and
- (iii) estimate the cumulative expected effect in that subsequent year of all of the factors identified in paragraph (e)(2)(i) on the estimated costs, volumes, and revenues of the Postal Service, relative to those presented for the first year of the agreement in response to paragraph (e)(1) of this section.

(f) *Impact analysis.* Every formal request shall include an analysis of the impact over the duration of the Negotiated Service Agreement on:

- (1) competitors of the parties to the Negotiated Service Agreement other than the Postal Service;
- (2) competitors of the Postal Service; and
- (3) mail users.

The Postal Service shall include a copy of any completed special studies that were used to conduct such analyses. If special studies have not been performed, the Postal Service shall state this fact and explain the alternate bases of its analyses.

(g) *Data collection plan.* Every formal request shall include a proposal for a data collection plan, which shall include a comparison of the analysis presented in § 3001.193(e)(1)(ii) with the actual results ascertained from implementation of the

Negotiated Service Agreement. The results shall be reported to the Commission on an annual or more frequent basis.

(j) Rejection of Requests **[As explained in the text of these comments, this paragraph should be omitted.]**

Rule 195 Requests to Recommend a Baseline Negotiated Service Agreement

(b) The Commission will treat requests predicated on a baseline Negotiated Service Agreement as subject to the maximum expedition consistent with procedural fairness. The schedule for adoption of a recommended decision will therefore be established, in each case, to allow for issuance of such decision not more than 150 days after the filing of the request of the Postal Service. Nothing in this section shall be construed to affect the rights of the Postal Service or other parties with respect to temporary implementation of changes pursuant to section 3641 of the Act.

Rule 196 Requests to Recommend a Negotiated Service Agreement That Derives Key Components from a Previously Recommended Negotiated Service Agreement.

(a) This section governs Postal Service requests for a recommended decision in regard to a Negotiated Service Agreement that includes key components from a Negotiated Service Agreement previously recommended by the Commission and currently in effect. The previously recommended Negotiated Service Agreement shall be referred to as the baseline agreement. The purpose of this section is to establish procedures that provide for accelerated review of derivative Negotiated Service Agreements. The Postal Service request shall include:

- (1) a detailed description of how the proposed Negotiated Service Agreement is, and is not, based on components of a baseline agreement;
- (2) identification of the record evidence from the baseline agreement docket, or any other previously concluded docket, on which the Postal Service proposes to rely, including specific citation to the locations of such evidence;
- (3) any available special studies developing information pertinent to the proposed Negotiated Service Agreement;

- (4) if applicable, the identification of circumstances unique to the request; and
- (5) if applicable, a proposal for limitation of issues in the proceeding, except that the following issues will be relevant to every request predicated on a functionally equivalent Negotiated Service Agreement:
 - (i) the financial impact of the Negotiated Service Agreement on the Postal Service over the duration of the agreement;
 - (ii) the fairness and equity of the Negotiated Service Agreement in regard to other users of the mail; and
 - (iii) the fairness and equity of the Negotiated Service Agreement in regard to affected markets.

(b) When the Postal Service submits a request derived from an existing Negotiated Service Agreement, it shall provide written notice of its request, either by hand delivery or by First-Class Mail, to all participants in the Commission Docket established to consider the baseline agreement. Any participant, not limited to those who appeared in a previous Docket, who intends to contend a particular issue in a derivative docket shall identify such issue(s) not later than 5 days before the pre-hearing conference.

(c) The Commission will schedule a pre-hearing conference for each request. Participants shall be prepared to address whether or not it is appropriate to proceed under § 3001.196 at that time. After consideration of the material presented in support of the request, and the argument presented by the participants, if any, the Commission shall promptly issue a decision on whether or not to proceed under § 3001.196. If the Commission's decision is to not proceed under § 3001.196, the docket will proceed under § 3001.195.

(d) The Commission will treat requests derived from an existing Negotiated Service Agreements as subject to accelerated review consistent with procedural fairness. If the Commission determines that it is appropriate to proceed under § 3001.196, a schedule will be established which allows a recommended decision to be issued not more than:

- (1) 60 days after the determination is made to proceed under § 3001.196, if no hearing is held; or
- (2) 120 days after the determination is made to proceed under § 3001.196, if a hearing is scheduled.

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing document in accordance with Section 12 of the Rules of Practice.

Nan McKenzie

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September 30, 2003