

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

Rules applicable to Baseline)
and Functionally Equivalent)
Negotiated Service Agreements)

Docket No. RM 2003-5

**Reply Comments of Discover Financial Services, Inc.
October 14, 2003**

Discover Financial Services, Inc. (“Discover”), files these reply comments pursuant to the Commission’s September 4, 2003, Notice of Proposed Rulemaking. 68 Fed. Reg. 52546 (Sept. 4, 2003).

As a preliminary matter, Discover supports the Postal Service’s use of “derivative NSA” as a descriptive category and urges the Commission to adopt it. See Postal Service Comments at 24. Discover will use the term “derivative NSA” throughout the remainder of these comments, rather than “functionally equivalent NSA.”

Overview

For the NSA process to function efficiently, the Commission must protect the NSA mailer, the Postal Service, the public, other mailers, and competitors—all at the same time. This is a challenging but achievable task. The linchpin to accomplishing this task is flexibility by the Commission, particularly in its procedural rules.

A number of parties—the OCA and NNA particularly—have suggested that the Commission include more rigidity in the NSA process, and have suggested approaches with across-the-board one-size-fits-all evidentiary standards. Discover respectfully

suggests that the Commission reject those suggestions as inappropriate and adopt a more tailored, NSA-specific approach.

NSA filings will come in a vast variety of sizes, shapes, and complexities. This will require the Commission to use an evidentiary review process based on the specifics of each contract. Any attempt to establish broad, substantive, evidentiary standards that purport to govern all NSA filings will straightjacket the process and exponentially increase the transaction costs experienced by the mailers. Increasing transaction costs will not only discourage large mailers from negotiating NSAs, but will preclude small and medium size mailers from seriously participating in the NSA process, as the comments of DNA *et. al.* and Pitney Bowes correctly point out. DMA *et al.* Comments at 6-7; Pitney Bowes Comments at 3. Discover agrees with the comments of Pitney Bowes that “The Commission’s determination of what constitutes an ‘adequate record’ for a particular NSA proposal should be informed by the unique circumstances and likely impact of the NSA proposal before it.” *Id.*

For example, while volume projections may be relevant and non-confidential in some NSA proceedings, they may be totally irrelevant in others, and highly confidential in yet others. Likewise, competitive impact may be relevant in some cases, but irrelevant in others. Indeed, as discussed below, Discover believes that competitive impact would be significant in only a handful of NSAs proceedings.

Comments of the Postal Service and Others

Rule 193(a)

Discover supports the modifications to Rule 193(a) recommended by the Postal Service. The modifications would reduce the possibility of extensive litigation over

whether customer-specific information could be created in the NSA process and the expense associated with doing so. Postal Service Comments at 4 and 5. This type of prolonged litigation—particularly when dealing with derivative NSAs—could create extensive delays in the NSA process despite the stated goal of increasing efficiency. While such complexity may be appropriate when the entire rate structure of the Postal Service—a \$70 billion institution—is under review, it is not appropriate when just one contract is the issue.

Evidentiary testimony will accompany every NSA filing. That testimony will create a sufficient evidentiary basis for the Commission to favorably recommend the NSA—or not—and the Commission can act accordingly. One of the questions the Commission will have to deal with is the fact that much mailer-specific data, including volume forecasts, simply may not exist, as most of the comments have pointed out.

In some cases, there will be budgeted data. Businesses run on budgets. They are real budgets, and they are budgets for which managers are held accountable. Often, the larger the business, the more precise the budgeting process. Budgeted numbers are real. Companies rely on them. Creditors rely on them. Lenders rely on them. The Commission can, and should, rely on them too.

Some participants in the NSA process might not be pleased with using budgeted numbers and might request that the Postal Service and NSA mailers somehow create “more” or better numbers. Two points must be made here. First, as noted above, no forecast—certainly no study—is more accurate than a corporation’s actual operational budget numbers for predicting future behavior. Second, creating a process where a participant can litigate cost estimates to develop mailer-specific data will allow an NSA

mailer's competitor to gain a competitive advantage by simply delaying the case. And the more delay in a case, the bigger the competitive advantage to the objecting party. It will also create an incentive for one company to try to gain a competitive advantage over another by obtaining non-public information about the NSA mailer. The Commission should avoid this scenario at all costs.

The question of confidentiality concerns raised by Discover and most other parties is critical. The Commission must keep in mind that the more detail that is requested about mailer-specific costs, the more one runs into substantial issues of confidentiality because obtaining specific data involves projections and disclosure of information at a level that is usually not public. If the Commission seeks to deeply delve into mailer-specific data, the Commission is likely to find itself dealing with litigants whose main purpose in the litigation is to uncover or gain access to competitor's proprietary information. That would make a mockery out of the NSA process and should be avoided at all costs.

Time Frame

Discover supports recommendation by the Postal Service's and the DMA *et al.* to include a 150 day time frame in rule 195 for baseline NSAs. Postal Service Comments at 22. DMA *et al.* Comments at 8-9. Short and focused proceedings that operate quickly and efficiently will be critical in keeping transaction costs down. Keeping transaction costs down is the key to the success of the NSA review process. The 150 day period should begin on the date of filing the NSA.

Rule 193(e)

With respect to the Postal Service's suggested changes to rule 193(e) dealing with the financial analysis that must accompany each NSA filing, Discover believes that the discussion in DMA *et al.*'s comments is instructive, and that even the Postal Service's proposed changes are too rigid. Discover suggests that the level of detail of evidentiary support necessary for each NSA should not be written into stone by regulation.

Discover realizes that the rules provide for waivers but the very notion of a waiver to a rule suggests that the rule is the norm and that waivers will be granted only in abnormal situations. As Capital One aptly put it, "in the great majority of the cases, the Postal Service and the parties are going to request waivers, claiming that the information is unavailable, that it cannot be produced without undue burden, and that it is inappropriate in the circumstances. Either exceptions to the Rule will have to become the Rule, or mailers will not pursue NSAs." Capital One Comments at 3.

Discover recommends that the rule simply state that "Every formal request shall include a sufficient analysis of the effects of the Negotiated Service Agreement on Postal Service volumes, costs and revenues" and let the details of each NSA dictate the type and level of financial analysis required.

Rule 193(f)

Turning to the Postal Service's discussion of impact, Discover believes that the Commission should simply substitute the word "discussion" for "analysis" and

“discussion” for “estimate” in its proposed rule.¹ The Postal Service’s comments on the implications of the notion of “estimate” are well-taken Postal Service Comments at 16.

As noted below, Discover believes that most NSAs will have very little impact on competition provided that competitors’ derivative NSAs are quickly approved. For instance, Discover believes that the Capitol One NSA will not have a significant competitive impact on the industry, so long as Capitol One’s competitors have an equal opportunity to quickly obtain a derivative NSA that meets the specific needs of their individual situations. An omnibus requirement more rigid than requiring a simple statement will only increase the transaction costs of the review process.

Derivative NSAs

Discover supports the Postal Service’s recommendation that participants identify the elements of the filing they intend to contest. This is very important in derivative NSAs, where the anti-competitive effect on a derivative NSA mailer will be the delay in the process of approving a derivative NSA. The Postal Service recommends a time frame of five days before the pre-hearing conference. Discover supports that recommendation.

In terms of the evidentiary standard for derivative NSAs, the Commission should never create the situation—or let participants create it—where a derivative NSA mailer must disclose confidential information in order to secure an NSA relatively equivalent to

¹ The text of the rule should read:

(f) Impact ~~analysis~~ discussion. Every formal request shall include ~~an estimate~~ a discussion of the impact . . .

* * *

The Postal Service shall include . . . that were used ~~to make such estimates~~ in its evaluation. If special studies . . . the alternate bases of its ~~estimates~~ conclusions.

that of its competitors, even if its competitor disclosed the same information in the baseline proceedings. Information may be more confidential to one company than to another and one company might be able to disclose information that its competitor might not be able to disclose. In a related issue, the Commission should be aware that extensive post-NSA data collection plans that provide information specific to one applicant could raise enormous competitive concerns.

Competitive Impact

A number of comments have raised the issue of competitive impact and the degree to which it should factor into the Commission's analysis. The issue has also received considerable Congressional attention over the years. In considering the matter, the Commission might wish to distinguish among several markedly different situations, as outlined below.

The first situation is where an NSA mailer is willing to perform extra work for the Postal Service in return for a share of the money saved by the Postal Service. While this scenario does not increase the volume of mail processed by the Postal Service, it does result in a significant cost savings to the Postal Service. The competitive impact of the proposal is not significant, so long as: 1) the Postal Service is willing to provide the competitors of the baseline NSA mailers with an equivalent "deal" in a derivative NSA, and 2) the Commission is willing to review the derivative NSA in an expedited manner that does not involve the imposition of extensive transaction costs on the competitive mailer(s), nor the exposure of confidential information. The greater the transaction costs, the more risk of competitive harm to smaller mailers. In this situation, a

competitive impact statement is not necessary and a fast, inexpensive, process will best serve the interests of the parties.

A second situation is where a non-cost-based declining block discount is provided to a mailer that is mailing its own pieces or its own advertising mail in order to increase its marketing efforts. This scenario is aimed at increasing volume and institutional contribution, and not decreasing costs. In this case, Discover believes there would be minimal competitive impact since the additional volume would be the mailer's "own" volume and not volume "taken" from another mailer. Like the first scenario, it is vital that the system allow competitors to quickly obtain an equivalent "deal" without revealing confidential information.

In a third scenario, a competitive impact could arise if a mailer receiving a baseline NSA mails not its "own" mail but mail consolidated from others. In this case,² lowering postage rates through non-cost-based declining block discounts could allow the baseline mailer to take mail away from its competitors. This would occur because the NSA mailer would be able to charge customers less than its competitors, who perform the same worksharing activity but who do not enjoy the competitive advantage of entering their mail with a declining block discount. In this scenario, a competitive impact analysis would be important, as would ensuring that the competitor to the baseline NSA mailer quickly receive an equivalent "deal."

² This scenario could occur if one mailing house received a non-cost-based declining block discount over its competitors, or one shopper or shared mailer received a non-cost-based declining block discount over its competitors.

Conclusion

Discover commends the Commission for proposing NSA-specific rules. The rules must be simplified, the burdens reduced, and confidential data kept confidential or the NSA process will not succeed. The Commission should realize that this process is quite different from a rate case, and requires extensive attention to confidentiality and to keeping transaction costs down.

Thank you for considering our views.

Respectfully submitted,

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