Postal Rate Commission
Submitted 6/15/2005 10:47 am
Filing ID: 44953
Accepted 6/15/2005

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

RATE AND SERVICE CHANGES TO IMPLEMENT FUNCTIONALLY EQUIVALENT NEGOTIATED SERVICE AGREEMENT WITH HSBC NORTH AMERICA HOLDINGS INC.	Docket No. MC2005-2

NOTICE OF THE UNITED STATES POSTAL SERVICE
OF DECISION OF THE GOVERNORS
(June 15, 2005)

The United States Postal Service hereby provides notice of the attached Decision of the Governors in Docket No. MC2005-2:

Decision of the Governors of the United States Postal Service on the Opinion and Recommended Decision of the Postal Rate Commission Approving Negotiated Service Agreement with HSBC North America Holdings Inc., Docket No. MC2005–2

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.
Chief Counsel, Ratemaking

Eric P. Koetting

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260-1137
(202) 268-2992, Fax -5402
June 15, 2005

DECISION OF THE GOVERNORS OF THE UNITED STATES POSTAL SERVICE ON THE OPINION AND RECOMMENDED DECISION OF THE POSTAL RATE COMMISSION APPROVING NEGOTIATED SERVICE AGREEMENT WITH HSBC NORTH AMERICA HOLDINGS INC., DOCKET NO. MC2005–2

June 14, 2005

STATEMENT OF EXPLANATION AND JUSTIFICATION

On May 20, 2005, the Postal Rate Commission issued its Opinion and Recommended Decision in Docket No. MC2005-2. The Commission recommended the rates and classification language, with very minor modifications, contained in the Postal Service's Request.[1] PRC Op. MC2005-2 at 42, 44. This language will enable the Postal Service to implement a negotiated service agreement ("NSA") that it signed with HSBC North America Holding Inc. ("HSBC").

Based upon our review of the record, we find that the Commission's recommended decision is reasonable and supported by substantial record evidence, and we approve the recommendations.

This case, following the Docket Nos. MC2004-3 (Bank One) and MC2004-4 (Discover) NSA cases, represented the third occasions for the Commission to apply Rule 196 for NSAs that are functionally equivalent to baseline NSAs, 39 C.F.R. § 3001.196. Specifically, the Commission found that the HSBC NSA was functionally equivalent to the Capital One NSA, which we considered in Docket No. MC2002-2. We appreciate the efficient manner in which this docket has been handled. In order for Negotiated Service Agreements to reach their full potential as innovative mechanisms to meet the

[1] Request of the United States Postal Service for a Recommended Decision on Classifications, Rates and Fees To Implement Functionally Equivalent Negotiated Service Agreement With HSBC North America Holding Inc., Docket No. MC2005-2 (February 23, 2005).

diverse needs of individual mailers, functionally equivalent cases will need to be handled expeditiously, as the cost of litigation is a major upfront expense for any mailer signing an NSA with the Postal Service. Less than three months elapsed from the date of filing of this case to the date of the recommended decision, a notable achievement representing a commendable effort by the Commission and the participants, and hopefully one setting a standard that can be matched in similar cases in the future.

BACKGROUND AND SUMMARY

The Postal Service initiated this proceeding on February 23, 2005, filing its Request in accordance with 39 U.S.C. §§ 3622 and 3623.

The Postal Service supported its Request with the written direct testimony of witness Jessica Dauer (USPS-T-1) and other documents. Also on February 23, 2005, HSBC, as a co-proponent, filed a notice of appearance, along with the written direct testimony of witness John Harvey (HSBC-T-1).

The Commission's Office of the Consumer Advocate ("OCA") and five intervenors participated in this proceeding. The co-proponents responded to discovery requests from the parties, as well as Presiding Officer's Information Requests. No participant requested a hearing, or chose to introduce testimony opposing the proposal. The co-proponents filed initial briefs in accordance with the Commission's scheduling order.

The Commission determined that this case would proceed under Rule 196 for functionally equivalent NSAs, and also granted a motion by the Postal Service, filed under that rule, to limit the issues in the proceeding to those related to financial and competitive aspects of the Request.[2]

EVALUATION AND RECORD SUPPORT

Under the terms of the NSA, HSBC agrees to acceptance of "electronic returns" of certain undeliverable-as-addressed ("UAA") First-Class Mail, in lieu of actual physical return of the pieces. This type of provision suits HSBC, as it did Capital One in Docket No. MC2002-2, because HSBC makes significant use of First-Class Mail to send

[2] Presiding Officer's Ruling No. MC2005-2/1, Docket No. MC2005-2 (March 29, 2005).

solicitations that advertise its credit card services. Electronic address correction service will provide HSBC with information about each undeliverable piece, rather than returning the advertising piece itself, for which HSBC has no further need. This change will result in cost savings for the Postal Service because the costs of providing the information electronically are lower than the costs of physical return of each UAA First-Class Mail solicitation piece.

In addition to the provisions regarding returns, the NSA also provides HSBC with the opportunity to pay lower "declining block rates," if it provides very high volumes of First-Class Mail (over 615 million pieces in the first year). Under this arrangement, HSBC potentially could have received discounts in the first year starting at 2.5 cents off each piece above 615 billion, up to 5.0 cents for each piece above 735 million. This provision is comparable to, but not identical with, the provision of declining block rates to Capital One in the baseline docket. The NSA will benefit all mailers because HSBC has committed itself to various measures that the Governors and Commission both conclude will reduce costs in a way that exceeds the cumulative value of the discounts. Also, the NSA will yield contribution from increased First-Class Mail volume.

In the instant docket, the Commission approved four new customer-specific terms within the proposed DMCS language that were not present in the Capital One NSA. The first such term is a series of discount threshold adjustments specifically negotiated for each year of the agreement, designed to keep alive, in the second and third years of the agreement, the incentives for HSBC to increase further its First-Class Mail solicitations against a backdrop of anticipated general volume growth for the company. The second and third customer-specific terms are closely related to the first. The second is an annual threshold adjustment mechanism, designed to calibrate (if necessary) the thresholds negotiated for the second and third years in light of actual volume growth in each preceding year. The third is another calibration mechanism, designed to increase thresholds for all three years based on the proportion of calendar year 2005 that has expired before the agreement is actually implemented.[3]

[3] In light of this third provision, and given the implementation date of November 1, 2005 set below, it bears mention that the threshold level for the first tier of discounts will not be 615 million pieces in the first year, 725 million pieces in the second year, and 810 million pieces in the third year, as would have been the case had the agreement been

(continued…)

The fourth customer-specific term is a negotiated cap of $9 million on the maximum cumulative discounts HSBC may receive over the life of the NSA. In accepting a discount cap set at this level, the Commission pointed specifically to the additional protections in the HSBC agreement afforded by the three other customer-specific adjustment mechanisms discussed above, and by its view that there may be more than one reasonable level for a cap, as long as it serves its intended purpose. PRC Op. MC2005-2 at 37-38. We have had differences with the Commission on the discount cap issue ever since the Capital One case, and those differences are currently being explored again in the Commission's reconsideration of the Bank One case (Docket No. MC2004-3). Our understanding, however, is that the Postal Service determined that the possibility of later resolution of the discount cap issue under more favorable terms did not provide sufficient reason to delay consideration of an NSA with HSBC under terms (including a discount cap) comparable to those currently being enjoyed by the three existing NSA partners. Under these circumstances, our approval of the cap negotiated with HSBC and recommended by the Commission does not represent any retreat from the views we have expressed previously on this broader issue, but is instead a pragmatic effort to maintain a level playing field for the Postal Service's customers in this industry. We are prepared to revisit this issue for HSBC, as well as the other NSA partners, as future developments warrant.

The record provides full support for the Commission's conclusion that the HSBC NSA is fair and equitable to other users of the mail, including competitors of HSBC. PRC Op. MC2005-2 at 38-40. We believe that the best way for issues of competition and undue discrimination to be addressed, in this context, is through notice and opportunity to be heard. As the Commission noted, no competitors of HSBC, or any other mailers, argued that this NSA was anti-competitive or unduly discriminatory. *Id.* at 39.

(...continued)
implemented in January of 2005. Instead, under the implementation date adjustment mechanism, those three figures increase to 707 million pieces in the first year, 796 million pieces in the second year, and 881 million pieces in the third year, with corresponding increases in all other discount tiers.

We agree with the Commission that the record supports the recommended changes in rates and classification, and we approve them. We concur with the Commission that its recommended decision is consistent with the policies of sections 3622 and 3623 of the Postal Reorganization Act. *See* discussion at PRC Op. MC2005-2, at 40-42.

Estimate Of Anticipated Revenue

The Postal Reorganization Act requires that our Decision include an estimate of anticipated impact on postal revenues (39 U.S.C. § 3625(e)). According to the evidentiary record, the Postal Service will benefit by $6.3 million over the life of the agreement -- $6.6 million in ACS Cost Savings, plus $4.1 million in increased contribution, minus $4.4 million in discount exposure (referred to in the Capital One proceedings as leakage).

Order

In accordance with the foregoing Decision of the Governors, the changes in rates and classifications set forth in the Attachments are hereby approved and ordered into effect. In accordance with Resolution 05-7 of the Board of Governors, dated June 14, 2005, these changes will take effect at 12:01 a.m. on November 1, 2005.

By The Governors:

James C. Miller III, Chairman

RESOLUTION OF THE BOARD OF GOVERNORS
OF THE
UNITED STATES POSTAL SERVICE
Resolution No. 05-7

Effective Date of Rate and Service Changes To Implement
Negotiated Service Agreement with HSBC North America Holding Inc.

RESOLVED:

Pursuant to section 3625(f) of Title 39, United States Code, the Board of Governors determines that the rate and service changes to implement the Negotiated Service Agreement with HSBC North America Holding Inc., that were ordered to be placed into effect by the Decision of the Governors adopted on June 14, 2005, shall become effective as follows: All changes will take effect at 12:01 a.m. on November 1, 2005.

The foregoing Resolution was adopted by the Board of Governors on June 14, 2005.

William T. Johnstone, Secretary

APPROVED CHANGES IN RATE SCHEDULES

The following represent the changes to the rate schedules recommended by the Postal Rate Commission and approved by the Governors of the Postal Service in Docket No. MC2005-2. The changes require the addition of four new rate schedules — 613A, 613B, 613C and 613D. The underlined text signifies that the text is new, and shall appear in addition to all other rate schedule text.

ATTACHMENT A

HSBC NORTH AMERICA HOLDINGS INC. NSA
RATE SCHEDULE 613A

(First Year of Agreement)

Volume Block	Incremental Discounts
615,000,001 to 655,000,000	2.5¢
655,000,001 to 755,000,000	3.0¢
675,000,001 to 695,000,000	3.5¢
695,000,001 to 715,000,000	4.0¢
715,000,001 to 735,000,000	4.5¢
735,000,001 and above	5.0¢

ATTACHMENT A

HSBC NORTH AMERICA HOLDINGS INC. NSA
RATE SCHEDULE 613B

(Second Year of Agreement)

Volume Block	Incremental Discounts
725,000,001 to 765,000,000	2.5¢
765,000,001 to 785,000,000	3.0¢
785,000,001 to 805,000,000	3.5¢
805,000,001 to 825,000,000	4.0¢
825,000,001 to 845,000,000	4.5¢
845,000,001 and above	5.0¢

ATTACHMENT A

HSBC NORTH AMERICA HOLDINGS INC. NSA
RATE SCHEDULE 613C

(Third Year of Agreement)

Volume Block	Incremental Discounts
810,000,001 to 850,000,000	2.5¢
850,000,001 to 870,000,000	3.0¢
870,000,001 to 890,000,000	3.5¢
890,000,001 to 910,000,000	4.0¢
910,000,001 to 930,000,000	4.5¢
930,000,001 and above	5.0¢

ATTACHMENT A

HSBC NORTH AMERICA HOLDINGS INC. NSA
RATE SCHEDULE 613D
FOR ADJUSTED THRESHOLDS (A.T.)

Volume Block	Incremental Discounts
(A.T.) to (A.T.+40,000,000)	2.5¢
(A.T.+40,000,001) to (A.T.+60,000,000)	3.0¢
(A.T.+60,000,001) to (A.T.+80,000,000)	3.5¢
(A.T.+80,000,001) to (A.T.+100,000,000)	4.0¢
(A.T.+100,000,001) to (A.T.+120,000,000)	4.5¢
(A.T.+120,000,001) and above	5.0¢

ATTACHMENT B

APPROVED CHANGES IN THE DOMESTIC MAIL CLASSIFICATION SCHEDULE

The following material represents changes to the Domestic Mail Classification Schedule recommended by the Postal Rate Commission and approved by the Governors of the Postal Service in Docket No. MC2005-2. The underlined text signifies that the text is new, and shall appear in addition to all other Domestic Mail Classification Schedule text.

NEGOTIATED SERVICE AGREEMENTS
CLASSIFICATION SCHEDULE

613 HSBC NORTH AMERICA HOLDINGS INC. NEGOTIATED SERVICE AGREEMENT

613.1 Eligible First-Class Mail

Eligible First-Class Mail under this section is defined as: (1) HSBC's First-Class Mail customer correspondence related to credit and banking products and services account holders; and (2) First-Class Mail solicitations for credit and banking products that bear an endorsement specified by the Postal Service. Eligible First-Class Mail does not include Business Reply Mail, Qualified Business Reply Mail, Cards, Priority Mail, or pieces that are not letter-shaped.

613.2 Waiver of Address Correction Fees

The fees for address correction in Fee Schedule 911 are waived for those First-Class Mail solicitations on which HSBC uses the endorsement specified by the Postal Service, if:

a. HSBC mails more than 525 million pieces of eligible First-Class Mail within the first year after implementation of this section, and

b. HSBC updates any databases it maintains for solicitation mail, other than First-Class Mail customer correspondence related to account holders, as specified by the Postal Service.

If, during the first year after implementation, HSBC mails fewer than 525 million pieces of eligible First-Class Mail, HSBC agrees to pay the greater of either (1) all address correction service fees under Fee Schedule 911, as specified by the Postal Service, for pieces receiving address correction service, or (2) $200,000.

613.3 First-Class Mail Discounts

613.31 Discount Thresholds. The First-Class Mail Volume Threshold is set at 615 million pieces of eligible First-Class Mail for the first year of the agreement, 725 million pieces for the second year of the agreement, and 810 million pieces for the third year of the agreement.

613.32 Discounts. HSBC's eligible First-Class Mail is subject to the otherwise applicable First-Class Mail postage in Rate Schedule 221, less the discounts shown in Rate Schedule 613A for the first year of the agreement, in Rate Schedule 613B for the second year of the agreement, and in Rate Schedule 613C for the third year of the agreement, if HSBC meets the applicable Discount Threshold in any of those years. The discounts apply in each year only to volume above the Discount Threshold for that year. Each incremental discount applies only to the incremental volume within each volume block.

613.33 Annual Threshold Adjustments. The discount thresholds specified in section 613.31 for the second and third years of the agreement may be adjusted upward or downward based on the relationship between mail volumes forecasted by HSBC for the first and second years of the agreement, and the mail volumes actually tendered by HSBC in those years. To determine whether any adjustment is warranted under this provision, at the end of the first and second years of the agreement, percentage deviations will be calculated between the before-rates forecasts of HSBC's First-Class Mail and Standard Mail volumes for the year, and HSBC's actual volume in each category. An upward adjustment will be triggered if the actual volume of First-Class Mail exceeds the forecasted volume by more than 20 percent, and the actual volume of Standard Mail exceeds the forecasted volume by more than 5 percent. For years in which the upward adjustment is triggered, the discount threshold specified in section 613.31 for the next year will be increased by a percentage amount equal to the First-Class Mail volume percentage surplus, less 15 percent. A downward adjustment will be triggered if the forecasted volume of First-Class Mail exceeds the actual volume of First-Class Mail by more than 15 percent. For years in which a downward adjustment is triggered, the discount threshold specified in section 613.31 for the next year will be decreased by a percentage amount equal to the First-Class Mail volume percentage deficit, less 15 percent. Any new annual threshold amounts calculated under this provision will be rounded to the nearest whole million pieces of mail. For any year for which a new annual threshold amount has been derived pursuant to this provision, Rate Schedule 613D will be applicable in lieu of Rate Schedule 613B or 613C.

613.34 Threshold Adjustment for Mergers and Acquisitions; and Portfolio Activity.

In the event that:

a. HSBC merges with and/or acquires an entity and/or purchases a portfolio with annual First-Class Mail volume in excess of 10 million pieces, the discount threshold will be adjusted to add the volume of First-Class Mail sent by the merged or acquired entity, or on behalf of the purchased portfolio, during the 12 months preceding the merger, acquisition, or purchase. In that event, beginning in the succeeding fiscal quarter immediately following the date that mail volumes due to the merger, acquisition, or purchase begin to be mailed through the threshold permit accounts, Rate Schedule 613D would apply in lieu of Rate Schedule 613A, 613B, or 613C.

b. HSBC in the first or second year of the agreement merges with or acquires multiple entities, or purchases multiple portfolios, that have combined annual First-Class Mail volume in excess of 25 million pieces, the discount thresholds for all succeeding years of the agreement will be adjusted upward to add the First-Class Mail volume sent by the merged or acquired entities, or on behalf of the acquired portfolios, for the 12 months prior to the date the mail of the merged entity is first mailed through the threshold permit accounts. In that event, in all succeeding years of the agreement, Rate Schedule 613D would apply in lieu of Rate Schedule 613B or 613C.

c. HSBC loses or sells a portfolio with annual First-Class Mail volume of at least 10 million pieces, the discount threshold will be adjusted downward by the product of the number of active accounts lost or sold, multiplied by 12. In that event, beginning in the succeeding fiscal quarter immediately following the date that the mail volumes due to the loss or sale will no longer be mailed through the threshold permit accounts, Rate Schedule 613D will apply in lieu of Rate Schedule 613A, 613B, or 613C.

d. In order to avoid double counting, any volumes used to make adjustments pursuant to these merger, acquisition, and portfolio activity provisions shall be excluded from calculation of the corresponding annual threshold adjustment pursuant to section 613.33.

613.35 Discount Limit. The maximum cumulative discount available to HSBC over the duration of this NSA shall not exceed $9 million.

613.36 Implementation Date Threshold Adjustments

The discount threshold specified in section 613.31 for the first year of the agreement shall be increased by the difference between the thresholds specified for the first year and the second year, pro-rated on a monthly basis from January 1, 2005, to the first day of the month of the actual date of implementation, and then rounded to the nearest whole million pieces of mail. The discount threshold specified for the second year of the agreement shall be similarly increased, by applying the same proportional factor to the difference between the thresholds specified for the second and third year. The discount threshold specified for the third year shall be increased by the same absolute amount of volume added to the threshold for the second year. Similarly, for purposes of determining any applicable annual threshold adjustments as specified in section 613.33, the before-rates forecasts of HSBC's First-Class Mail for the first and second years of the agreement shall be increased by applying the same proportional factor to the differences between, respectively, the before-rates forecasts for the first and second years, and the before-rates forecasts for the second and third years.

613.4 Rates

The rates applicable to this Agreement are set forth in Rate Schedules 613A, 613B, 613C, and 613D.

613.5 Expiration

The provisions of section 613 expire on November 1, 2008.

613.6 Precedence

To the extent any provision of section 613 is inconsistent with any other provision of the Domestic Mail Classification Schedule, the former shall control.

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 and Procedure.

Eric P. Koetting

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260–1137
(202) 268-2992, FAX: -5402
June 15, 2005
eric.p.koetting@usps.gov