

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

Rate and Service Changes to Implement)
Baseline Negotiated Service Agreement with)
Bookspan)
_____)

Docket MC2005-3

Reply Brief of
Discover Financial Services, LLC (DFS)
December 15, 2005

DFS hereby submits its reply brief in this case.

Predictably, several briefs have raised questions about the legality of the NSA, the volume projections of the NSA, and the profitability of the NSA. DFS is confident that the co-proponents of this NSA will rebut those arguments in their reply briefs, and DFS will not address these arguments.

This brief addresses three points raised by the APWU and OCA in their briefs that cannot be left unchallenged. These points concern whether parties negotiating NSAs should be able to rely on current Postal Service data, whether there is value in the complexity of the negotiation process, and whether advertising mail is being increasingly challenged by other channels.

I.
The APWU's Data Quality Argument

The APWU generally urges the Commission to reject this NSA because the "quality" of the underlying data is not "good enough" to legally justify it, despite the fact

that this same data is “good enough” to legally justify the rates that will go into effect on January 8, 2006. Specifically, the APWU states:

the cost data it [the Postal Service] has submitted is so deeply flawed as to be useless for the purpose of determining the effect of this NSA. . . . the Postal Service cannot demonstrate that the predicted gain can be realized because the cost data for both standard letters and standard flats are inaccurate.

APWU Brief at 5 and 6. To justify its position, the APWU revisits issues raised in the recently-concluded rate case, and criticizes the Postal Service's witness in this case, Witness Yorgey, for not investigating and adjusting her data to compensate for alleged flaws. To support its arguments, the APWU cites to Postal Service witnesses' answers to interrogatories both in this case and in the last rate case. See *Id.* at 7-8.

If the quality of any data is good enough to legally justify new rates, it has to be good enough to legally justify an NSA based on those rates. Any other result would be arbitrary and capricious, and would create chaos in the NSA negotiating marketplace. This is because, if the NSA process is to function effectively, parties negotiating NSAs need to be able to rely on the data used by the Commission to legally justify the rates that an NSA will key on, as they talk with the Postal Service.¹

Finally, to allow any party to come into an NSA case and challenge the quality of data that was accepted in the last rate case would be to allow any party to re-litigate issues from the last case, or perhaps “pre-litigate” issues from the next case.² The Commission should not permit such a spectacle for it would not only waste limited Commission resources, but also drive up the transactions costs of obtaining NSAs.

¹ DFS must stress that it takes no position on the merits of the data issues raised by the APWU, but simply states that the data underlying the current rates—which has been legally accepted by the Commission—must be an acceptable basis for an NSA if the NSA process is to work.

II. The OCA's Desire to Stop the Negotiating

The OCA suggests that one of the major problems with the NSA process is that the negotiating process is too lengthy and complex. OCA Redacted Brief at 39. Further, the OCA seems to think that the solution to this problem is for the Postal Service to stop negotiating and revert back to a system where it would “treat its customers anonymously.” Id. at 41. Implicit in the OCA's position is the supposition that “negotiating” with mailers is a “flawed” process that should be avoided at all costs.³

But DFS suggests that the exact opposite is true. Complex and lengthy discussions tend to form complex and robust bonds, based upon a complex and profound mutual understanding. The more this process happens between mailers and the Postal Service, and the more mailers that become involved in this process, the better it is for all.

Years ago mailers sharply complained about the anonymous postal managers who worked in the isolated ivy tower of L'Enfant Plaza. These were postal managers who did not understand how their customers' business worked, had no idea what their customers' actual business needs were, and were completely clueless about what their customers' future needs might be. As a result, postal managers often took actions that needlessly harmed their customers businesses, or inhibited their growth. This hurt not

² Were the Commission to hold that certain data were not “good enough” to support an NSA, would that not also, effectively, be a holding that that the data were not “good enough” to support the rates currently (or soon-to-be) in effect? Would that be tantamount to finding that the current rates are illegal?

³ See *e.g.*, OCA Redacted Brief at 6 (“Better yet, these pricing mechanisms involve no negotiations.”)

only the mailers, but the Postal Service. This anonymity was deeply inculcated in the postal culture, and it took years to drive it out.

Apparently the OCA would have the Postal Service put it back in. That is to be avoided. Today the Postal Service is acting like a business. Part of acting like a business is doing what all businesses due with their customers—learn about their customers and their businesses in part by negotiating over price and products. That is to be encouraged, not discouraged.⁴

One of the most important by-products of the evolution of the NSA process is that the Postal Service has spent hours upon hours negotiating with scores of mailers in many different industries, in an attempt to gain a sophisticated understanding of those businesses and those industries. The goal has been to figure out a way for the Postal Service to help those businesses grow in a fashion that also benefits the Postal Service.⁵

The Postal Service's time has been well spent in this endeavor, for the result of that process has been a spike in the level of sophistication of the Postal Service in understanding its customers and their businesses, particularly when compared to ten or twenty years ago. This would be true even if no NSAs had resulted.

Today the Postal Service is justifiably proud of the focus on the customer that it has put at the forefront of its priorities and that it has made a major part of its

⁴ For years, Congress has been saying that the Postal Service needs to pay more attention to its customers and needs to act more like a business. Indeed, one of the underlying predicates of the current postal reform movement is to try to force the Postal Service to act more like a business. See, e.g., Press Release of Chairman Tom Davis, "The Need for Postal Reform." December 7, 2004 ("This legislation will force the Postal Service to act more like a business.")

⁵ This too appears to be a goal that the OCA just doesn't accept. See OCA Redacted Brief at 41 (seller may be better off if it ignores information about a buyer's past decisions).

Transformation Plan.⁶ That evolution is a very positive development, and it should be encouraged in all respects—including negotiating with mailers, which should be expanded.

III. Competition from Other Channels

At page 41 of its brief, the OCA states: “Both declarations pointed to the need for regulated utilities to meet competition by offering special deals to customers who threaten to leave.” It then says: “The Postal Service faces no such threats. There are no close substitutes for direct mail advertising, . . .” *Id.*

There is no record evidence in this docket to support such a proposition. There is, however, ample record evidence in this docket and every other NSA docket to refute it.⁷ As shown in the material cited in footnote seven, the parties that have negotiated NSAs have testified, from slightly different perspectives, that 1) that they understood and used advertising mail extensively, 2) that they valued advertising mail, 3) that

⁶ See, e.g., United States Postal Service Strategic Transformation Plan, 2006-2010, at page 1 (Message from the Chairman of the Board, James C. Miller III and Postmaster General & CEO, John E. Potter): “We will promote growth by creating more value for every customer.” See also page 9 (creating more customer value through products and services as a transformation strategy.)

⁷ See generally Bookspan transcript at Tr. 3/379-380, 395, 444 (“The percentage that each media represents in our overall marketing portfolio shifts, largely depending on price and relative effectiveness. These media are priced very differently, and there are vast differences in the effectiveness of the various channels.”); Capital One transcript at Tr. 2/39, 130-131, 171 (“ . . . those are factors that are considered in deciding between first class, standard, as well as other marketing channels, like the Internet or telemarketing.”); Discover Financial Services transcript at Tr. 2/33-34, 37-39 (“While mail provides many benefits, this channel does face increasing competition. . . . Moreover, unless the cost structure for mail becomes more attractive, this trend will continue in years two and three, as alternate channels increasingly are considered by DFS.”); Bank One transcript at Tr. 2/41-42, 119, 124, 130-131, 137 (“We also developed successful new marketing channels that do not rely on direct mail, which is becoming increasingly more expensive and less effective.”); HSBC transcript at Tr. 2/20-22, 35, 53-56 (“Mail is one of several channels available for marketing financial services, and faces increasing competition from alternatives, such as E-mail and the Internet, event marketing, merchant marketing, telemarketing, print, television, radio, and outdoor advertising.”).

advertising mail was being increasingly challenged by other advertising channels, and 4) that this competition from other channels would increase.

How the OCA could make the statements quoted above, given the depth and breadth of this testimony throughout the NSA dockets, is beyond DFS' comprehension. Apparently the OCA just does not understand that day in and day out, every week of every year, marketing departments throughout the country are making decisions, largely based on price and effectiveness, between direct mail and other marketing channels—particularly electronic ones. Moreover, the OCA just does not understand that direct mail increasingly is on the losing end of many of those decisions. The OCA needs to accept this fact, and adjust its approach accordingly.

Conclusion

The Commission should reject the APWU and OCA arguments discussed above, for the reasons discussed herein.

Respectfully submitted,

/S/

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