

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

POSTAL RATE AND FEE CHANGES

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Docket R 2006-1

DIRECT TESTIMONY
OF
MARY PAT RESCH
ON BEHALF OF
DISCOVER FINANCIAL SERVICES LLC
AND
MORGAN STANLEY, INC.

September 6, 2006

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My name is Mary Pat Resch. My title is Vice President of Administration and Processing Services for Discover Financial Services LLC, (DFS) which is a business unit of Morgan Stanley, Inc. My testimony today is from the DFS perspective, and is given on behalf of DFS.

I. PURPOSE OF TESTIMONY

The purpose of my testimony is to support the Postal Service's proposal to reduce the First-Class additional ounce rate, to give a real life perspective of what the results of that proposal will be on the industry, and to urge the Commission to approve the proposal.

II. QUALIFICATIONS AND BACKGROUND

My responsibilities at DFS are diverse. Included among the functions that report to me are processing services, facilities, procurement, and corporate travel. Processing services encompasses the printing and mailing of all Cardmembers and merchant statements and letters, the embossing and mailing of the actual plastic cards we issue, and the processing of the payments we

1 receive. In this role, I am directly responsible for all non-marketing mail. I was
2 part of the team that negotiated the DFS NSA with the Postal Service. In my
3 facilities role, I am responsible for the design, construction, and maintenance of
4 all of DFS' facilities, including the two facilities that we mail from in Tennessee
5 and Utah.

6 I have been in my present position for 6 years, and I have been with
7 Discover (or its predecessor) for 15 years. During that time, I have run the
8 collection, fraud, and recovery groups in the call centers, worked in marketing,
9 and directed a variety of special projects. Before coming to the financial services
10 industry, I worked in operations for Marshall Field's in Chicago.

11 With more than 50 million Cardmembers, DFS is one of the largest issuers
12 of credit cards in the U.S. We issue a variety of Discover® Card credit cards,
13 and offer other financial services. Over the years DFS has pioneered many card
14 features that have spread throughout the industry—no annual fee, 24/7 customer
15 service, and the Cashback Bonus® award.

16 DFS is one of the largest mailers in the country, and mails both Standard
17 and First-Class. As is typical of a large mailer, DFS is a member of a number of
18 trade associations that are parties in this case. These include the American
19 Bankers Association, the Major Mailers Association, the Association for Postal
20 Commerce (Postcom), and the National Postal Policy Counsel.

21 The monthly mailing of our Discover Card statements, plastics, and letters
22 comprise the majority of our First-Class mailings. These mailings are typical of
23 the mailings of the financial services industry. Our invoice mailings are also

1 typical of other companies that have monthly billing cycles in industries such as
2 telecommunications, insurance, and public utilities.

3 **III. SUMMARY OF MY TESTIMONY**

4 Due to the high level at which the First-Class additional ounce rate has
5 been priced, DFS has always managed its mail to one ounce, a practice for
6 which I am responsible. Assuming the Commission approves the Postal
7 Service's additional ounce proposal, we will modify that practice and seriously
8 explore how we can better use additional ounce mail.

9 In this testimony I describe the business opportunity that the lowering of
10 the additional ounce rate will create for us, and how we will react to that. I also
11 point out that DFS' reaction should be typical of companies that mail bills and
12 statements.

13 My testimony further concludes that this business opportunity should
14 result in a transformation of the nature of our statement mailings and add a
15 significant marketing component to it. The addition of this marketing component
16 should, to some degree, slow the rate of the diversion of our statements from the
17 mail to electronic delivery.

18 **IV. THE POSTAL SERVICE'S ADDITIONAL OUNCE PROPOSAL**

19 For years, DFS has managed the mail to one ounce. We did that because
20 we wanted to ensure that DFS would not be burdened by paying additional
21 ounce postage on our Cardmember statements and letters. If the Commission
22 approves the Postal Service's additional ounce proposal, we will modify that
23 practice and look to increase our additional ounce mail.

1 In this vein, DFS hopes that the Commission approves this proposal, as
2 do the ABA, NAPM, MMA, NPPC, and the other mailing organizations that are
3 concerned with First Class. The Postal Service's proposal will grant us some
4 long overdue relief on this front.

5 While I do understand why First-Class rates are higher—for example, the
6 service is expected to be faster, the mail is sealed against inspection, and
7 forwarding is included at no extra charge—I have never understood the
8 enormous difference in rate treatment for First-Class and Standard Mail letters
9 that weigh more than an ounce. In Standard Mail, the rates don't go up at all
10 until one reaches the weight break at 3.3 ounces. Yet in First-Class, rates
11 increase immediately after the first ounce.

12 That hasn't made any sense, particularly when both First-Class and
13 Standard letters are processed on the same machines. If there is little difference
14 in costs between one and two ounce Standard Mail letters, how can there be a
15 significant difference in costs between one and two ounce First-Class letters?

16 **V. INDUSTRY REACTION TO THE LOWERING OF THE**
17 **ADDITIONAL OUNCE RATE**

18
19 Lowering the additional ounce rate will create a unique business
20 opportunity for those who mail invoices and statements. Since the postage for
21 an additional ounce of automation mail will be 15.5¢, a mailer will be able to
22 enclose one or more marketing pieces in its statement much more readily than it
23 can now. These marketing pieces could be the company's own marketing
24 pieces, designed to target its existing customers. Alternatively, these marketing
25 pieces could be from another company, and designed to target the first

1 company's customers. The nature of the marketing dynamic would all depend
2 upon the situation, the pieces, and the company.

3 For DFS, we have made a decision not to insert other company's
4 marketing pieces into our statements. Thus anything we will insert into our
5 statement mail generally will be a Discover Card piece or a co-branded piece. I
6 would expect that other companies would not necessarily follow that practice, but
7 would use pieces from other companies. Indeed for some companies, adding
8 inserts tailored to their customers needs could enhance the product and the
9 billing experience.¹

10 I cannot estimate the frequency with which DFS will use this opportunity,
11 nor how many pieces we will insert into our statement mail. These are decisions
12 that will be made on a case-by-case basis, and the dynamic is so new that one
13 simply cannot predict such things in advance with any accuracy. I can describe,
14 however, the type of analysis that our marketing department will go through when
15 it does face those decisions.

16 First, since any piece, by definition, will be directed at our customers, it will
17 be a targeted effort, perhaps even demographically or psychographically sub-
18 targeted.² Moreover, DFS would not only consider inserting separate pieces, but
19 would consider reformatting our bills to include advertising messages, knowing
20 that this will take our statements above one ounce. For instance, we could add

¹ For example, a monthly invoice to a military book club member could contain a piece or pieces marketing military memorabilia; a monthly invoice to a science-fiction book club member could contain a piece marketing Lord of the Rings memorabilia; a monthly invoice to a spiritual book club member could contain a piece marketing a spiritual retreat. The possibilities are endless.

² Demographic targeting is targeting by characteristics such as age, sex, income, etc. Psychographic targeting can easily be thought of as targeting by behavior, which is caused by individual preferences, attitudes and value systems.

1 an additional page to market our Cashback Bonus program to the right customer,
2 or include some other cross-product promotion.

3 Second, since the price break of the additional ounce rate (15.5¢) will be
4 lower than the price break for either a Standard Mail piece (23.5¢ at the 3 digit
5 level) or a separate First Class piece (33.1¢ at the 3 digit level), this proposal
6 gives our marketers a new and less expensive alternative for our marketing
7 messages to reach our targets. Further, since the message would ride along
8 with our bill, that would probably have to be taken into account in designing the
9 message. This should create new alternatives for marketing messages that we
10 would not otherwise have mailed.

11 Finally, since our targets are our existing customers, we will be extremely
12 sensitive not to burden them with too many messages in one mailing, or with
13 messages that they will not want. In this respect, our marketing department will
14 have to analyze each mailing to see how many messages will be in that mailing,
15 what they are, how they relate to one another, and what messages have gone
16 out in the past. Moreover, in doing all this, we will be very careful not to dilute
17 our Discover brand. It will be an interesting set of analytics.

18 DFS' reaction to the business opportunity the Postal Service's additional
19 ounce proposal will create should be typical of companies that regularly invoice.
20 While the specific analytics will be different,³ the result will be the same in the
21 sense that companies should start to make greater use of heavier First-Class
22 mail, and thus volume in the "First-Class additional ounce" category—with its still

³ A company's specific analytics will depend upon the product or service being marketed, the company's customers, and its marketing philosophy.

1 high contribution to overhead—should go up. My understanding is that, even at
2 15.5¢ per piece, given the minimal costs of additional ounce mail, this new “First-
3 Class additional ounce mail” will be extremely profitable for the Postal Service.

4 **VI. EFFECT OF THE POSTAL SERVICE’S PROPOSAL ON**
5 **STATEMENT MAILING**

6 As I noted earlier, DFS has traditionally managed its mail to one ounce
7 because of the level of the additional ounce rate. Should this new proposal be
8 adopted, that no longer would be true, as I have discussed above.

9 That means that, as we decide whether to take our statement delivery
10 electronic, we will have to evaluate marketing considerations as well as billing
11 considerations because of the opportunities that additional ounce mail has
12 created. For those companies that are willing to insert the material of others into
13 their invoices, this proposal would additionally create a new and perhaps
14 significant revenue opportunity for them. Consequently, these companies would
15 have to consider revenue gains and losses, in their electronic diversion
16 deliberations, in addition to marketing and billing considerations.

17 Overall, these opportunities will add a new dimension to First-Class bill
18 and statement mail, and change the analysis for diverting statements to
19 electronic delivery. Put another way, the net effect of this proposal would be to
20 give bill and statement mailers an economic incentive to keep statement mailings
21 in the mail. This is because, for each statement that would be diverted to
22 electronic delivery, the company would lose the ability to mail a marketing piece

1 for 15.5¢, a much smaller investment than mailing a solo mail piece at Standard-
2 Mail rates (23.5¢) or First-Class rates Piece (33.1¢).⁴

3 Finally, I do not want to overstate this last point. The Postal Service's
4 proposed lowering of the additional ounce rate is unlikely to reverse the trend
5 towards electronic diversion of statement delivery. It would, however, temper
6 that diversion and keep tens if not hundreds of millions of dollars of contribution
7 in the Postal Service coffers.

8 **VII. CONCLUSION**

9 The Postal Service's additional ounce proposal provides a new and
10 significant business opportunity for all invoice mailers that should transform the
11 nature of statement mailings. That transformation will create economic
12 incentives to keep statement mail in the system by adding a significant marketing
13 component to it. The addition of this marketing component should, to some
14 degree, temper the rate of electronic diversion of statements, and for these
15 reasons we urge the Commission to approve it.

16 Thank you.

⁴ Assuming a 3-digit sort.