

REDACTED (PUBLIC) VERSION

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Rate and Service Changes to Implement)
Baseline Negotiated Service Agreement) Docket No. MC2007-1
With Bank of America Corporation)

**REPLY POST-HEARING BRIEF OF
BANK OF AMERICA CORPORATION**

Stacey Stone Bennett
Assistant General Counsel
Global Staff Support Functions
BANK OF AMERICA, N.A.
101 South Tryon Street
NC1-002-29-01
Charlotte, NC 28255
(704) 388-6583
stacey.stone_bennett@bankofamerica.com

David M. Levy
Richard E. Young
SIDLEY AUSTIN LLP
1501 K Street, N.W.
Washington, DC 20005-1401
(202) 736-8000
dlevy@sidley.com
ryoung@sidley.com

Counsel for Bank of America Corporation

August 13, 2007
Revised August 14, 2007

CONTENTS

INTRODUCTION AND SUMMARY.....	1
ARGUMENT	4
I. THE NSA OFFERS MAJOR BENEFITS TO THE POSTAL SERVICE.	4
A. APWU <i>et al.</i> Have Failed To Establish That The Current Read/Accept Rates Of BAC Mail Are Higher Than Those Indicated By The System-Average Data Accepted By The Commission In R2006-1.	6
1. Reliance on system-average data on read/accept rates is entirely proper.	6
2. The untested recent data seized upon by the NSA opponents are not better evidence of BAC's baseline read/accept rates than the system-average data relied on by the Commission in R2000-1 through R2006-1.	15
B. The Proposed NSA Would "Benefit The Postal Service" Within The Meaning Of Rule 190(b) Even If BAC's Current Read-Accept Rates Were As High As APWU <i>et al.</i> Contend.	22
C. The Expiration Of The Postal Service's Authority To File A Traditional Rate Case On December 20, 2007, Will Insulate Other Mailers From Even The Theoretical Possibility That The Loss Of Contribution From An NSA Could Result In Higher Rates On Other Services.	29
D. Adjustments To The Baseline Read/Accept Rates Negotiated By BAC And The Postal Service Would Reduce The Economic Incentive For BAC To Invest In Improved Performance, And Could Jeopardize The Entire NSA.	31
E. Implementation Of The Commission's Pricing Rules Under PAEA Will Render The Objections Of APWU, OCA And Valpak Moot By Allowing USPS To Implement This Or Any Other NSA On Only 45 Days Advance Notice – And With None Of The Costly And Intrusive Advance Review That BAC And The USPS Have Endured Here.	34

F.	The Notion That The Commission Should Micro-Manage The Profitability Of This NSA Is Hopelessly At Odds With The Recognition By APWU <i>et al.</i> That PAEA Warrants A Hands-Off Approach To The Pricing Of Competitive Services.....	36
II.	OTHER LEGAL CHALLENGES TO THE NSA ARE WITHOUT MERIT.....	36
	CONCLUSION.....	40

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Rate and Service Changes to Implement)
Baseline Negotiated Service Agreement) Docket No. MC2007-1
With Bank of America Corporation)

**REPLY POST-HEARING BRIEF OF
BANK OF AMERICA CORPORATION**

The Bank of America Corporation (“BAC”) respectfully submits its reply post-hearing brief in this case. This brief responds to initial briefs of the three opponents of the proposed Negotiated Service Agreement (“NSA”): American Postal Workers Union, AFL-CIO (“APWU”), Office of Consumer Advocate (“OCA”), and Valpak Direct Marketing Systems, Inc., and Valpak Dealers’ Association, Inc. (“Valpak”).

INTRODUCTION AND SUMMARY

The initial briefs of APWU, OCA and Valpak confirm the lack of any cogent argument against the proposed NSA. The NSA opponents argue, in essence, that: (1) current data indicate that mail processing performance is higher than indicated by the 1999 data relied on by the Postal Service to set the baseline levels for the mail processing performance discounts in the NSA; (2) the NSA thus will not “benefit the Postal Service” within the meaning of Rule 190(b), 39 C.F.R. § 3001.190(b); and (3) the NSA therefore must be rejected in its entirety (APWU and Valpak) or the aggregate discounts paid over the three-year term of the NSA must be capped at \$8.3 million, which are the total savings assumed to

occur from reduced forwarding and return rates alone (OCA). Each link in this chain of reasoning is unsound.

First, the NSA opponents have offered no evidence that the proposed discounts for improved mail processing performance would make the Postal Service worse off, even if these NSA elements were evaluated in isolation. The NSA baseline values rest on system average data repeatedly found appropriate to set billions of dollars of worksharing discounts in omnibus rate cases, most recently in R2006-1, without challenge by APWU, OCA, Valpak or any other party. Those data, not the subsequent data proffered by the NSA opponents, are the best evidence of BAC's current baseline performance.

Second, the requirement that the NSA provide a net financial "benefit" to "the Postal Service" must be applied to the NSA as a whole, not to individual components of the NSA in isolation. The NSA opponents do not even attempt such a showing. Given the wide range of benefits that the NSA will provide to the Postal Service, such an outcome would be highly implausible.

Third, the Postal Service's authority to justify rate increases by reference to overall revenue shortfalls expires pursuant to 39 U.S.C. § 3622(f) on December 20, 2007—barely four months from now. This fact eliminates the fundamental predicate for the Commission regulatory concern over the contribution from NSAs. With the contribution from NSAs delinked from rates for any other mail, no NSA, no matter how improvident, could cause other mailers to pay higher rates.

Fourth, adjusting the negotiated baseline read/accept rates would reduce the economic incentive for BAC to invest in improved performance, and could jeopardize the entire NSA.

Fifth, the relief sought by the NSA opponents will be moot within a few months. The more flexible regulation mandated by PAEA for NSAs and other forms of rate discounting will allow the filing of similar NSAs without the time-consuming, costly and burdensome regulatory oversight that has prevailed under the prior law.

Likewise, the interventionist role which APWU *et al.* urge the Commission to take here is flatly inconsistent with the light-handed regulation they have (correctly) advocated in Docket No. RM2007-1 regarding downward pricing flexibility for other market-dominant and competitive services having far greater financial effect on the Postal Service than NSAs have.

For these reasons, BAC respectfully requests that the Commission recommend the proposed NSA without modification. BAC also requests that the Commission issue its decision expeditiously. More than six months have passed since the filing of the proponents' Request in this case. Further delays will create additional barriers to the implementation of the NSA. BAC's fiscal year ends in December, and funding the projects needed to implement the NSA will be more difficult if the NSA is not implemented by then. Moreover, many of the third-party vendors needed to design and install the systems required to implement the process changes mandated by the NSA have been unwilling to do so while its regulatory status remains unresolved. For all of these reasons, BAC respectfully

requests that the Commission issue its recommended decision as expeditiously as the record, and the Commission's docket, permit.

ARGUMENT

I. THE NSA OFFERS MAJOR BENEFITS TO THE POSTAL SERVICE.

The initial briefs of BAC and the Postal Service described the numerous benefits that the NSA would provide the Postal Service. These benefits fall into two general categories.

First, BAC would commit its annual letter mail volume of more than three billion pieces to serve as a large-scale pilot and test bed for the Postal Service's new Intelligent Mail technologies. Specifically, BAC would agree to use Intelligent Mail Barcodes, Confirm® service, OneCode ACS, FAST, eDropship, Seamless Acceptance, and postage payment through the Centralized Automated Payment System ("CAPS"). These commitments, taken collectively, would require a very large mailer, for the very first time, to use all the productivity-enhancing tools that the Postal Service currently plans for the network of the future. Enabling the Postal Service to move more quickly up the learning curve toward full-scale deployment of Intelligent Mail technology would benefit much of the Postal Service's customer base. BAC Br. 10-13, 23-24; USPS Br. 1, 18-23, 26-28.

Second, the NSA would offer BAC discounts for optional process changes that produce quantifiable improvements in the read/accept rates of BAC letter mail, the return and forwarding rates of Undeliverable-As-Addressed ("UAA")

First-Class Mail, and the disposal rates of UAA Standard Mail. Because the discounts offered by the Postal Service would pass through less than 100 percent of the unit cost savings, the Postal Service would benefit from these pay-for-performance rate incentives regardless of the magnitude of the improvement in performance. BAC Br. 13-18; USPS Br. 16-18; Jones Direct (BAC-T-1) at 1; Tr. 71-73 (Ayub response to OCA/USPS-T1-4); Tr. 131-133 (Ayub response to OCA/USPS-T1-31).

With one exception, the participants opposing the NSA dispute *none* of these benefits. The exception involves the proposed pay-for-performance discounts for improvements in mail processing performance. APWU *et al.* assert that recent data indicate that current read/accept rates are already higher than baseline levels indicated by the 1999 data on which the Postal Service relied; hence, the proposed rate discounts would cost the Postal Service money by requiring it to pay BAC for performance that BAC would achieve anyway. APWU Br. 3-5 & Table 2; OCA Br. 7-9; Valpak Br. 8-13. APWU and Valpak contend that this supposed deficiency warrants rejection of the NSA in its entirety. APWU Br. 5; Valpak Br. 8, 13, 22. OCA would cap the NSA discounts at \$8.3 million over the three-year term of the NSA—a restriction that would render the NSA uneconomic for BAC, and therefore have the same effect as outright rejection. OCA Br. 1, 9-10.

Each link of this chain of reasoning is unsound. We discuss in turn: (1) the record evidence submitted by both sides on BAC's current mail processing performance; (2) the net benefits to the Postal Service from the multiple

provisions of the NSA as a whole; (3) the effect of 39 U.S.C. § 3622(f) on any remaining concerns that other mailers might have to pay higher rates if the contribution from this NSA were to be negative; (4) the consequences of capping the NSA discounts as proposed by OCA; and (5) the likelihood that that the challenges to the NSA advanced by APWU *et al.* will become moot when the rules implementing the ratemaking standards of PAEA take effect later this year.

A. APWU *et al.* Have Failed To Establish That The Current Read/Accept Rates Of BAC Mail Are Higher Than Those Indicated By The System-Average Data Accepted By The Commission In R2006-1.

1. Reliance on system-average data on read/accept rates is entirely proper.

The initial briefs confirm that the 1999 system average data on read/accept rates used by the Postal Service to calculate baseline performance levels for the proposed mail processing performance discounts are the best available evidence of record of BAC's baseline performance. Ample precedent supports the use of system-average data to estimate mailer-specific cost inputs when (as here) mailer-specific data are unavailable. BAC Br. 27-30; USPS Br. 24-26. APWU, OCA and Valpak have offered no cogent argument to the contrary. We discuss the arguments of each participant in turn.

APWU. APWU does not dispute the appropriateness of using non-mailer specific data. APWU's position is entirely reasonable, since the alternative data that APWU would have the Commission rely on (discussed below) are also system average, or at least non-BAC specific.

OCA. OCA first suggests that system average data can *never* be used as a surrogate for mailer-specific data. OCA Br. 2 & nn. 3-4 (asserting that the NSA proponents cannot satisfy their burden of proof because USPS witness Ayub admitted that BAC-specific read/accept rates are not known “at this time”). OCA does not even attempt to distinguish, however, the consistent chain of Commission and judicial precedent upholding the use of system-average data and other surrogate data in this circumstance—including the Capital One and Discover NSA decisions, in which the Commission specifically upheld the use of system average data *even where the record indicated that system average data overstated the actual unit cost savings to the Postal Service from changed mailer practices.*¹

Second, OCA contends that, regardless of whether system-average data could be used in some circumstances, BAC and the Postal Service have waived their right to use such data by failing to submit a formal request for waiver under Rule 193(a)(2)-(3). OCA Br. 4 n. 14. OCA gains nothing with this appeal to formalism. Rule 193(e)(1)(v) specifically provides that:

If mailer-specific costs . . . are not available, the bases of the costs . . . that are proposed shall be provided, including a discussion of

¹ See BAC Br. 28-29 (citing cases); MC2002 PR Op. & Rec. Decis. ¶¶ 6011-6019, 6053, 8031 (use of system average data to estimate the savings from ACS provisions and waiver of physical return of Capital One’s UAA mail); MC2004-4 Op. & Rec. Decis. at 29 (accepting use of a generic ACS success rate in lieu of Discover-specific value); see also MC2004-3 PRC Op. & Further Rec. Decis. (Apr. 21, 2006) at ¶ 5011 (proposing to base Panzar formula for volume discounts on “inputs already used in rate cases, thus ameliorating the difficulties inherent in litigating the accuracy of mailer-specific volume forecasts before the Commission”).

the suitability of the proposed costs . . . as a proxy for mailer-specific costs

39 C.F.R. § 3001.193(e)(1)(v). BAC and the Postal Service complied with this rule by explaining in detail why mailer-specific data on BAC's Before Rates read-accept rates were unavailable, and why system average data were a suitable proxy.² Having complied with Rule 193(e)(1)(v), the NSA proponents had no need to seek a waiver of its requirements under Rule 193(a)(2)-(3)—just as no waiver of Rule 193(e)(1)(v) was sought, or granted, in the instances cited above when the Commission accepted system-average data as a surrogate for mailer-specific data.³

Third, OCA's claim that system-average data are inapplicable to BAC because BAC is not an "average mailer" (OCA Br. 3-4) confuses mail volume with mail processing performance. The issue is not whether BAC's *mail volume* is higher than average, but whether BAC's *mail processing performance* is better than average. There is no evidence that the latter is true. The vast majority of BAC mail is prepared by the same third-party vendors that other large mailers

² See BAC Br. 26-30 & nn. 11-17 (citing record).

³ In any event, the Postal Service specifically reserved the right at the outset of this case to seek a waiver of any filing requirement subsequently found to be unsatisfied by the Commission. Request at 6 & Attachment E-1. If the Commission somehow were to find that the formality of a waiver request under Rule 193(a)(2)-(3) were necessary, BAC and the Postal Service hereby submit such a request *nunc pro tunc*. OCA can hardly claim any unfairness from such relief, since it was aware of the issue of system-average data for read/accept rates from virtually the outset of the case, and elected not to raise the waiver issue until now.

use.⁴ Moreover, the record also indicates that most BAC mail, by virtue of its entry deep into the Postal Service network, is likely to have *worse* mail processing performance than the average mail from other mailers, most of which is entered upstream in the network, and is groomed of unreadable addresses and barcodes upstream before reaching the downstream points where most BAC mail is entered and processed.⁵

Fourth, OCA's insistence that BAC and the Postal Service could have determined BAC-specific read/accept rates by performing a special study (OCA Br. 6) is utterly at odds with the record. The obstacles go beyond the likelihood that such a study would prompt allegations that BAC was trying to low-ball the baseline values by submitting poor quality mail during the study, although that certainly would have been a likely objection from the NSA opponents.⁶ The record demonstrates that:

⁴ See Tr. 144 (Ayub response to OCA/BAC-T1-35); Tr. 486 (BAC answer to APWU/USPS-T1-1(b)); Tr. 488 (redacted version of BAC answer to APWU/USPS-T1-8).

⁵ See BAC Br. 34-35; USPS Br. 29-30; Tr. 403 (Ramey response to APWU/USPS-ST3-5).

⁶ OCA's suggestion that no one would have raised such an objection (OCA Br. 6 & n. 26) is particularly ironic. This is the same OCA that asserted that "The possibility that BAC's read rates will be below the baseline can be safely ignored" because "the fact that BAC has agreed to the use of a 1999 baseline sends a strong signal that BAC expects to exceed that baseline." OCA Comments in Response to NOI No. 1 (Apr. 17, 2007) at 1.

- BAC does not use Four-State Barcodes⁷ on letter-rated First-Class Mail or Standard Mail.⁸
- Only about half of BAC statement mail currently has a POSTNET barcode, and less than one percent of BAC mail has a PLANET barcode.
- In any event, neither of these existing symbologies has sufficient fields to carry the information needed to determine mailer-specific read/accept rates.⁹
- Further, BAC does not currently enter its mailings with mail.dat files or other information needed to enable the Postal Service to determine the denominator of the read/accept ratio.¹⁰
- For these reasons, it is not possible for the Postal Service to measure or calculate read/accept rates specific to BAC.¹¹

OCA makes no mention of these obstacles. In the real world, however, they cannot be evaded by being ignored.

Finally, OCA's assertion that the failure of BAC and the Postal Service to conduct a special study to estimate the "2007 [sic] average" accept rate of "printers used by BAC" before filing this case warrants an "adverse inference"

⁷ The Postal Service also describes Four-State Barcodes as "Intelligent Mail Barcodes" or "IMB". BAC, like the Postal Service, will use the terms interchangeably herein.

⁸ Tr. 71-73 (Ayub response to OCA/BAC-T1-4); Tr. 479 (Jones response to OCA/BAC-T1-4(a)).

⁹ See Ayub Direct (USPS-T-1) at 5, 8, 16; Tr. 98-100 (Ayub response to OCA/USPS-T1-14); Tr. 273 (Ayub response to VP/USPS-T1-3(d)).

¹⁰ See Ayub Direct (USPS-T-1) at 11:7-8; Tr. 253 (Ayub response to VP/USPS-T1-6). The costs of generating and submitting mail.dat or similar files would be "significant" for BAC. *Id.*

¹¹ Ayub Direct (USPS-T-1) at 16.

that the such a study would yield values higher than the 1999 system average values (OCA Br. 7) is frivolous. The “adverse inference” rule applies when a party in control of evidence that already exists unjustifiably fails to produce it.¹² The putative data described by OCA, by contrast, not only do not exist, but could not be created without a significant expenditure of time and resources by the Postal Service, BAC’s printers, and *their* other customers.¹³ None of BAC’s printers or their other customers are parties in this case, and none therefore could be compelled to participate in such a study. Given these perfectly legitimate reasons for not attempting such a study, the “adverse inference” rule simply does not apply.¹⁴

¹² See, e.g., *Everest Capital Ltd. v. Everest Funds Mgt., L.L.C.*, 393 F.3d 755, 761 n.3 (8th Cir. 2005) (“The adverse inference rule applies only ‘when a party has relevant evidence *within its control* which it fails to produce’”) (emphasis in original; citation omitted); *Ammex, Inc. v. United States*, 56 Fed. Cl. 1, 18 (Fed. Cl. 2003), *aff’d in part, rev’d in part on other grounds*, 384 F.3d 1368 (Fed. Cir. 2004), *cert. denied*, 544 U.S. 948 (2005) (adverse inference rule applied where plaintiff failed “to justifiably explain [its] failure” to produce records which, according to plaintiff’s president and operations manager, either existed or might exist).

¹³ See, e.g., Tr. 370 (Ayub).

¹⁴ See, e.g., *Evans v. Robbins*, 897 F.2d 966, 970 (8th Cir. 1990) (adverse inference rule is applicable only when, *inter alia*, “it appears that that the documentary evidence exists or existed” and “it appears that there has been actual suppression or withholding of evidence”); *Perricone v. Clarke*, 1999 WL 124477 (E.D. Pa. 1999) (denying plaintiff’s motion to apply adverse inference rule to defendants for their failure to produce incident reports, because reports were not in defendants’ control at the time they were lost or destroyed, and “the party that prevented production of the reports is not a party to this lawsuit”); *In re Hopson Marine Transportation, Inc.*, 168 F.R.D. 560, 566 (E.D. La. 1996) (refusing to apply adverse inference rule to defendant’s refusal to allow inspection, because rule “does not apply when there is no *wrongful* denial of discovery,” and court had upheld defendant’s grounds for objecting to discovery) (emphasis in original); *Atlantic Sugar, Ltd. v. United States*, 553 F.Supp. 1055,

(footnote continued on next page)

Valpak. Valpak, in contrast to OCA, acknowledges that “no mailer-specific data are available for BAC’s read/accept rate.” Valpak Br. 8. Valpak speculates, however, that BAC or the Postal Service could have used MERLIN data as a surrogate for BAC-specific data on read/accept rates (Valpak Br. 10 ¶ c). The record refutes this conjecture. Neither the Postal Service nor BAC knows the MERLIN scores of BAC’s mail.¹⁵ Indeed, BAC employees have not even received MERLIN training.¹⁶ The majority of BAC’s mail is produced by third-party vendors, who have neither the obligation nor the incentive to reveal to BAC the MERLIN scores of mail entered by those vendors, and who in any event would be unable to provide BAC-specific scores for the BAC component of mail entered as part of a multi-mailer comailing.¹⁷ Similarly, mail produced internally by BAC has its POSTNET barcode applied by third-party presort suppliers. BAC does not have on-site mail acceptance at any location.¹⁸ In any event, although high MERLIN scores tend to correlate positively with high read/rate performance,

(footnote continued from previous page)

1059 (C.I.T. 1982), *rev’d on other grounds*, 744 F.2d 1556 (Fed. Cir. 1984) (where sugar refiner did not have information concerning refinery for period before its acquisition of plants, failure of refiner to supply such information did not give rise to adverse inference). *Cf. Bashir v. Amtrak*, 119 F.3d 929, 931 (11th Cir. 1997) (adverse inference will be drawn from party’s failure to preserve evidence “only when the absence of that evidence is predicated on bad faith”).

¹⁵ Tr. 65 (Ayub response to APWU/USPS-T1-9(b)); Tr. 487 (BAC response to APWU/USPS-T1-3(b)).

¹⁶ Tr. 486 (BAC response to APWU/USPS-T1-2(a)).

¹⁷ Tr. 65 (Ayub response to APWU/USPS-T1-9(b)); Tr. 487 (BAC response to APWU/USPS-T1-3(a)).

¹⁸ *Id.*

“because the MERLIN standards differ from those used to measure read and accept rates, the observed read and accept rates can differ.”¹⁹

Valpak’s claim that the Intelligent Mail Barcode “is ready for mailer adoption at this writing” and that “in the very near future mailer-specific read/accept rates should be available for a large number of major mailers as soon as they adopt the other prerequisites” (Valpak Br. 12-13 ¶ i) is both irrelevant and untrue. What *other* mailers might do with Intelligent Mail Barcodes in the future is irrelevant because the NSA co-proponent whose baseline read/accept rates are at issue is BAC, not some other mailer, and BAC has not adopted IMBs.²⁰ BAC has no intention of voluntarily incurring the substantial systems development and investments needed to use the IMB without compensation from the Postal Service.²¹ Without IMBs on BAC mail, there are no IMB-based data on the processing performance of BAC mail for the Commission to consider.

In any event, Valpak’s rosy portrayal of Intelligent Mail Barcode technology as ready for full-scale “mailer adoption at this writing” is unsupported by the record. Valpak concedes that mailers are not now required to use Intelligent Mail Barcodes; will not be required to do so until at least 2009; and currently receive “no compensation from the Postal Service” to cover the costs of

¹⁹ Tr. 65 (Ayub response to APWU/USPS-T1-9(b)).

²⁰ Tr. 495-98 (BAC response to APWU/USPS-T1-32(b)).

²¹ *Id.*

adopting such barcodes voluntarily. Valpak Br. 12-13 ¶ i. Moreover, the scaling up of technology as innovative as the Intelligent Mail Barcode from small-scale beta tests to large-scale industry-wide usage is almost never trouble-free. As PMG Potter testified before a Senate oversight committee earlier this month, “My expectation is once that comes to pass, there are going to be a lot of problems because I’m sure that there are deficiencies in our system.”²² The proposed NSA would be of great value to the Postal Service in detecting, diagnosing and curing these problems—but only if BAC is given an adequate financial incentive to play such a role.

Finally, Valpak’s speculation that BAC’s mail processing performance somehow *must be* better than the system average because BAC self-selected to participate in the NSA (Valpak Br. 10 (¶ b)) is nonsensical. One could argue with equal logic that BAC’s baseline mail processing performance must be *worse* than the system average because the Postal Service chose BAC, rather than some putatively better-managed mailer, as its NSA partner. In the real world, however, parties enter into contracts without perfect knowledge of baseline conditions out of a belief that the *changes* in post-contract performance induced by the contract incentive terms will make *both* parties better off.

²² Testimony of the Honorable John E. Potter before the Senate Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security (Aug. 2, 2007).

2. The untested recent data seized upon by the NSA opponents are not better evidence of BAC's baseline read/accept rates than the system-average data relied on by the Commission in R2000-1 through R2006-1.

APWU, OCA and Valpak fare no better in their alternative argument that the system average data relied on by BAC and the Postal Service have been rendered obsolete by more recent system-average (or non-BAC) data indicating that current read/accept rates are now higher. APWU Br. 3-4; OCA Br. 5-7; Valpak Br. 9, 11-12. The premise of this argument appears to be little more than the proposition that newer data are better than older data. See OCA Br. 5 nn. 17-18; *id.* at 6-7. This proposition is clearly simplistic. While more recent data, all other things being equal, are generally better than older data, the qualification “all other things being equal” is crucial. As the Commission has noted:

Proposed analyses do not improve upon established ones simply because the underlying data are more current. Data must not only be current, but be reasonably free of both sample error and reporting error. The data must be of a kind that can be translated into meaningful econometric variables. The data also must be modeled in a way that makes theoretical sense, and yield results that are consistent with operational experience.

PRC Op. & Rec. Decis. R2005-1 (Nov. 1, 2005) at ¶ 4032.

Another important factor is whether the data, new or old, have been tested in the crucible of litigation. The 1999 system average data relied on by the Postal Service have been accepted by the Commission—without challenge by any participant—as an input to billions of dollars of worksharing discounts in omnibus rate cases since Docket No. R2000-1, including Docket No. R2006-1.

BAC Br. 30; USPS Br. 24-25. This testing entitles the data, at a minimum, to a presumption of reliability. BAC Br. 31.

None of the more recent data offered into the record overcome the presumption of reasonableness for the data relied on by the NSA proponents, or warrant the adoption of higher baseline values. We discuss in turn (1) the results of comparative tests of competing models of Wide Field-of-View barcode readers under consideration for purchase by the Postal Service about six years ago; (2) data generated by three recent pilot tests of the use of Intelligent Mail Barcodes by other mailers; (3) and end-of-run report data. BAC Br. 30-34; USPS Br. 24-25, 31-37.²³

Tests of the Wide Field-Of-View Barcode Reader in 2001-2003. APWU (but not OCA or Valpak) urges the Commission to rely on a table from a Decisional Analysis Report (“DAR”) in 2001 to show that “improvements in

²³ Valpak also speculates that baseline read/accept rates somehow must have improved as a result of the Postal Service’s efforts to educate mailers about good mailing practices (Valpak Br. 11 (¶d)) and the Postal Service’s investments in more modern barcode readers since 1999 (Valpak Br. 11-12 (¶¶ e and g)). The record provides no support for either conjecture, however. Education alone, without financial incentives, will not induce most mailers to make process changes that are highly costly. Tr. 283 (Ayub response to VP/USPS-T1-20). And the Postal Service’s investments in investments in barcode readers since 1999 have been designed primarily to improve read/accept rates for hand-written addresses and other low-quality addresses not at issue here, or to provide capacity to read additional data fields. Tr. 144, 271-74, 292-93 (Ayub). The record provides no evidence that these investments have caused the barcoded mail used by BAC to achieve read/accept rates higher than those adopted by BAC and the USPS as their proposed discount baselines in this case. *Id.*

read/accept rates from the WFOV camera of .45 percent for First Class Mail and 1.09 percent for Standard Mail” were “expected” by the authors of the DAR. APWU Br. 3-4. The record demonstrates, however, that the DAR projection has no probative value as evidence of the baseline performance of BAC mail.

First, the accept rates collected by the tests were not intended to be used as a basis for setting rates, a use that would require data on *absolute* accept rates, but rather were intended for the comparative exercise of determining which vendor’s model performed best *in comparison to the competing vendors’* models. Tr. 411 (Raney answer to APWU/USPS-T1-1 at 5).

Second, the competitive test was conducted “under controlled conditions that do not necessarily reflect the real world conditions under which BAC’s mail processing performance will be measured and evaluated.” *Id.* For example, technicians for the vendors were permitted to “conduct routine preventative maintenance and corrective maintenance on the equipment during the test”; were “encouraged to have ample spare parts to support their [WFOV] systems during the entire [test period]”; and were given a procedure for “mak[ing] hardware, software, and cabling improvements to the WFOV camera systems during the test.” Tr. 411-412 (Raney answer to APWU/USPS-T1-1 at 5).

Third, data were reported for only a selected subset of about 10 percent of the pieces for which data were collected during each week. Moreover, vendors were given “pretests” and a week of “fine-tuning” before the “formal test period commenced.” Tr. 412 (Raney answer to APWU/USPS-T1-1 at 5).

Fourth, pieces rejected for mechanical reasons were excluded from the data used to generate the reported results. USPS Br. 31-32.

The special treatment given to the vendors and their equipment in the test, the obvious competitive incentives of the vendors to tweak their equipment to obtain the best possible results, and the exclusion of data on pieces rejected for mechanical reasons may be entirely appropriate for tests that are designed to compare the performance of rival models of equipment under controlled conditions. But the resulting data cannot be regarded as probative evidence of actual read/accept rates under the shop floor conditions in which mail is processed in the ordinary course of business by the Postal Service today. BAC Br. 31-32.

APWU (understandably) does not mention at all these limitations on the applicability of the DAR results to this case.

Pilot test of Intelligent Mail Barcodes with three other business mailers. OCA and Valpak (but not APWU) urge the Commission to rely on mail processing performance data recently generated by three other Postal Service customers in relatively small-scale pilot tests of the Intelligent Mail Barcode. OCA Br. 5-6, 9; Valpak Br. 11 ¶ f. Like the Wide Field-of-View tests, however, the pilot tests overstate the read/accept rates that barcodes from mailers like BAC are likely to achieve in the ordinary course of business. BAC Br. 32-33; USPS Br. 32 n. 106.

First, the scan rates in the pilot tests were not based on the same definition of “read/accept” as the NSA. “Pieces could be scanned” within the meaning of the pilot test reports “without being read and accepted within the meaning of the NSA, and vice versa.” Tr. 42 (Ayub response to APWU/USPS-T1-4).

Second, high-profile pilot studies of this kind are often viewed by the participants as an opportunity to showcase both the new technology and the skill of the study participants at mastering it. For this reason, participants in these studies often devote more resources to maintenance, alignment, cleaning and calibration than might be expected with a mature technology used in the ordinary course of business. Tr. 141-42 (Ayub answer to OCA/USPS-T1-35).

Third, the pilot test results were based on an unrepresentative *subsample* of the mailpieces that was produced by *excluding* mailings with a MERLIN success rate below 95 percent. This selection process obviously skewed the results upward, because barcode readability is one of the grounds for rejection of mailpieces by MERLIN, and high MERLIN pass rates correlate with high scan rates. *Id.* at 142 (citing <http://ribbs.usps.gov/files/mtac/merlinbc.doc>); Tr. 155 (USPS *Seamless Acceptance Pilot* (Feb. 20, 2007), p. 8). BAC Br. 33; USPS Br. 33.

Moreover, despite all the special attention, the scan rates from the pilot tests represent only a marginal improvement over the older values. The weighted average scan rate of the three study participants—97.14 percent—is

barely higher than the baseline scan rates of 96.8 and 96.9 percent. *Id.* BAC Br. 34; USPS Br. 33.

Equally significant is the *variation* in performance among the three participants, with scan rates ranging from 96.88 percent for mailer C to 97.28 percent for Mailers A and B. *Id.*; see also Tr. 145-47 (Attachment A to Ayub response to OCA/USPS-T1-35). This variation refutes the notion that the mere use of Intelligent Mail Barcodes is a magic bullet that produces higher read/accept rates without additional care and effort by the mailer. To the contrary, a variety of factors can cause the barcodes on automation letters to fail to be read and accepted. Tr. 117-19 (Ayub response to OCA/USPS-T1-27) (enumerating causes). Overall, there is no reason to believe that the deployment of Intelligent Mail Barcodes has had a “measurable increase in the read/accept rates of First-Class Mail or Standard Mail letters.” Tr. 206 (Ayub answer to OCA/USPS-T1-37). BAC Br. 35.

OCA completely ignores all but the second of these points (that equipment vendors participating in a competitive test of equipment under consideration for purchase are likely to give their equipment special attention). OCA brushes off the latter point as “speculation,” OCA Br. 5-6, but offers nothing to counter the common-sense observation of USPS witness Ayub that vendors have a rational incentive to behave in this fashion.²⁴ Valpak does not discuss at all the conceptual problems with extrapolating the pilot test results to BAC.

²⁴ Tr. 141-42 (Ayub answer to OCA/USPS-T1-35).

End-of-Run Reports. APWU (but not OCA or Valpak) contends that the best evidence of current read/accept rates appears in a proprietary table of “actual National DBCS BCS read/accept rate data” for calendar year 2006. APWU Br. 4. Substituting these values for the values from USPS-LR-110.xls relied on by the Postal Service, APWU contends that the appropriate baseline read rates for First-Class Mail and Standard Mail, respectively, are **[BEGIN USPS PROPRIETARY]** **[END USPS PROPRIETARY]** rather than 96.77 percent and 96.87 percent. APWU Br., Table 2.

For the reasons previously explained by BAC and the Postal Service in their initial briefs, however, the baseline read/accept rates of BAC mail are almost certainly lower than the scan rates reported by the end-of-run reports for the average mail at a comparable stage in the network. The reason is that average accept rates in operations where mail is predominantly processed for the first time tend to be lower than in operations where mail has already been run multiple times upstream on the Postal Service’s automated equipment. Because BAC’s mail mix is predominantly 3-digit and 5-digit, BAC’s automation mail is likely to bypass upstream operations and receive its first scan in a downstream mail processing operation. As a result, BAC’s mail is more likely to experience lower-than-average accept rates than mail processed in the same operation that has been previously processed and accepted in an upstream operation, since the mail mix in downstream operations would presumably exclude pieces that were already processed and rejected upstream. BAC Br. 35 (discussing Tr. 403 (Raney answer to APWU-ST3-5); USPS Br. 29-30 (same)).

APWU is well aware of this issue, having tried at length to undermine Mr. Raney's testimony on this point during cross-examination. See Tr. 457-461. Under the circumstances, APWU's failure even to acknowledge the issue in its initial brief is telling.

B. The Proposed NSA Would “Benefit The Postal Service” Within The Meaning Of Rule 190(b) Even If BAC’s Current Read-Accept Rates Were As High As APWU *et al.* Contend.

Approval of the proposed NSA without modification would be warranted even if the Commission were to find that the baseline read/accept rate for BAC mail should be higher than the baseline values agreed to by BAC and the Postal Service. In resolving claims that a proposed NSA may not be contribution-positive for the Postal Service, the Commission must consider the profitability of the NSA as a whole, rather than focus on any one discount term in isolation. The only “association” required between the discounts received by the mailer and the benefits received by the Postal Service is that the *aggregate* benefits of all kind received by the Postal Service under the NSA must exceed the *aggregate* costs incurred by the Service in return.²⁵ In terms of Rule 190(b), which the NSA opponents assert is controlling, an NSA must “benefit the Postal Service.” 39 C.F.R. § 3001.190(b). Neither Rule 190(b), nor any other Commission rule,

²⁵ BAC Br. 25; USPS Br. 35; MC2002-2 PRC Op. & Rec. Decis. at ¶¶ 3058, 8006, 8010 (holding that the relevant dimension of profitability is the overall profitability of the NSA as a whole, not any individual component); Order No. 1391, *Negotiated Service Agreements*, 69 Fed. Reg. 7574, 7577-78, 7580 (2004) (same); MC2004-4 PRC Op. & Rec. Decis. at 52 (same).

requires that each *component* of an NSA, evaluated in isolation from every other component, must *individually* “benefit the Postal Service.”²⁶

None of the NSA opponents have offered any evidence that the proposed NSA, taken as a whole, would fail to offer positive net benefits to the Postal Service *even if the existing read/accept rates were higher than the negotiated baseline*. BAC Br. 26; USPS Br. 26-27 (listing other BAC commitments), 35-36. Moreover, such an outcome would be highly implausible.

As an illustration, assume for the sake of argument (and contrary to the evidence discussed above) that the current read/accept rates were actually a full percentage point higher than the baselines derived by BAC and the Postal Service from LR-110 (i.e., the data relied on without objection by the Commission

²⁶ The Commission specifically considered and rejected such a standard when adopting the current NSA rules in Docket No. RM2003-5. In that rulemaking, OCA asked the Commission to adopt the following language in lieu of what is now the first sentence of Rule 190(b):

It shall be the policy of the Commission to recommend Negotiated Service Agreements *each of whose elements are* consistent with statutory criteria, unambiguously benefit the Postal Service, and do not cause unreasonable harm to the marketplace.

Order No. 1391, Docket No. RM2003-5, *Negotiated Service Agreements*, 69 Fed. Reg. 7574, 7577 (col. 3) (2004) (emphasis added). The Commission rejected the OCA proposal as “too restrictive”:

Requiring each element to benefit the Postal Service could hinder this give and take process, and eliminate many possible arrangements from consideration.

Id. at 7577-7578.

to set worksharing discounts in Docket No. R2006-1 and several previous omnibus rate cases).²⁷ And assume further that BAC's After Rates read/accept performance *did not improve at all* above this higher baseline. In this event, BAC would receive discounts of about \$9.2 million at its projected volumes in the first year of the agreement for mail processing improvements, even though the Postal Service would obtain no savings from this component of the agreement.²⁸ This scenario illustrates the undesirable outcome that APWU and other NSA opponents predict from the NSA.

Now, however, vary the previous example by assuming that BAC also increased its read/accept rate by one percentage point above the higher baseline assumed in the example. Although the discounts received by BAC would grow to \$16.9 million (discounts are capped at an improvement of 1.9 percent percentage points),²⁹ the Postal Service would receive cost savings of more than \$13.7 million, including savings from the barcoding of Courtesy Reply Mail and

²⁷ This assumed value would also be higher than the performance indicated by the WFOV reports and the data from the current pilot tests of Intelligent Mail Barcodes. See pp. 16-20, *supra*.

²⁸ See Comments of BAC in Response to NOI #1 (filed April 17, 2007), Exh. 2, row labeled "1.9%," column 3.

²⁹ *This risk mitigation feature bears special emphasis.* The NSA caps the discounts for improvements in read/accept rates at an improvement of 1.9 percentage points, so even if the baseline read/accept rates were higher than the values assumed by BAC and the Postal Service, *BAC could not gain any additional discounts for any improvements, real or purported, in the read/accept rates beyond a maximum improvement of 1.9 percentage points.* NSA §§ IV.C.1 and IV.F.1.

Business Reply Mail envelopes.³⁰ In this scenario, the Postal Service's first-year reduction in contribution from the read/rate discounts would shrink to \$3.2 million *even without regard to any of the other benefits of the NSA.*

Moreover, those other NSA benefits almost certainly would outweigh this small hypothetical shortfall in contribution:

- For example, even a 20 percent improvement in forwards and returns for First-Class Mail would net the Postal Service a contribution of about \$424,000 (using USPS mail processing variability methods), and an additional \$83,000 or so in additional revenues from Confirm.³¹
- Further, with a 20 percent improvement for Standard Mail UAA, the savings plus the ACS revenue exceed the discounts by about \$1.8 million. Thus, at a 20 percent improvement in

³⁰ These figures can be derived from Exhibit 2 of BAC's Response to NOI #1 (filed April 17, 2007) by subtracting total savings at 1 percent improvement (row labeled 1%, column (6) value = \$16,093,065) from total savings at 1.9 percent improvement (row labeled 1%, column (6) value = \$28,626,028), and adding extrapolated savings from 2 percent improvement over 1.9 percent improvement (row labeled 1.9%, column (6), value = \$28,626,028, minus row labeled 1.8%, column (6), value = \$27,456,518, for a net result \$1,169,510. (For ease of calculation, this analysis makes the simplifying assumption that the difference between 2 percent and 1.9 percent improvement is the same as the difference between 1.9 percent and 1.8 percent improvement.)

³¹ See Excel spreadsheet attached to Ayub response to OCA/USPS-T1-4 (filed March 2, 2007), worksheet marked "Passthrough" (Tr. 43). The contribution may be calculated by subtracting incentives from cost savings at 20% improvement for First-Class Mail UAA for Operations Returns, Marketing Returns, and Forwards and adding the results—i.e., Cell (5C-5B)+(5F-5E)+(5I-5H)+51f. The projection of \$83,000 in Confirm revenue was based on the Confirm rates requested by the Postal Service in R2006-1. Although the Confirm fees recommended by the Commission differed, BAC believes that the number of additional CONFIRM identifiers it would buy to implement the NSA would render the \$83,000 revenue figure conservative.

addressing, the agreement increases USPS contribution by about \$2.3 million in the first year of the agreement.³²

- If the same percentage of BAC mail requires personal knowledge to complete delivery (“PKR” mail) as the Postal Service’s systemwide percentage for each class, then BAC PKR mail imposes costs of over \$2 million annually on the Postal Service. If BAC address improvements reduce the PKR rate by ten percent, the Service will save over \$200,000 annually; if the rates are reduced by 50 percent, the savings will be over \$1 million per year. BAC comments on NOI #1 (April 17, 2007) at 15-16.

An important lesson to draw from these calculations is that the contribution from the addressing quality components of the agreement, along with the absence of any discounts for (1) reducing PKR mail or (2) placing Four-State Barcodes on CRM, BRM and QB RM mail, provide the Postal Service with a considerable margin of safety. As a result, BAC’s company-specific Before Rates read/accept rates would have to be considerably higher than system average read/accept rates for the NSA to reduce the Postal Service’s contribution from BAC mail. In fact, the NSA would be contribution positive for the Postal Service as long as BAC’s actual improvement in read/accept performance (compared with BAC’s actual company-specific baseline) was slightly more than *half* the improvement in performance indicated by use of the Postal Service’s system-average read/accept baseline. See BAC response to NOI #1, Exhibit 2.

³² See spreadsheet attached to Ayub response to OCA/USPS-T1-4 (filed March 2, 2007), worksheet marked “Passthrough” (Tr. 43). Contribution calculated by subtracting incentive from cost savings at 20% improvement for Standard UAA and adding ACS—i.e., Cell C17-B17+E17.

Finally, even if the aggregate effect of all of the above discounts and benefits were still a net reduction in the Postal Service's net short-term contribution, that shortfall would be a bargain when balanced against the long-term benefit to the Postal Service from the availability of more than three billion pieces of BAC letter mail as an R&D test bed for all of the Postal Service's Intelligent Mail technologies. The Postal Service invested approximately \$41 million in R&D in Fiscal Year 2006, not including the amounts spent by its vendors.³³ Intelligent Mail technologies collectively offer one of the most significant and revolutionary transformations of the postal system since the establishment of the Postal Service by the Postal Reorganization Act of 1970. Is the Commission prepared to find that an additional expenditure of even several million dollars on what is essentially an R&D project for Intelligent Mail, with BAC as the test subject, would be so facially unreasonable and imprudent that Postal Service management should be denied the discretion to make such an investment? APWU, OCA and Valpak certainly cite nothing in the record to suggest that the Postal Service and its customers should be denied such an opportunity.

OCA's rejoinder that that most of the proposed benefits of the NSA to the Postal Service should be disregarded because BAC agreed to them as a "quid pro quo for the discounts [BAC] obtained" (OCA Br. 3 n. 6) is incomprehensible. It is certainly true that all of the commitments offered by BAC to the Postal

³³ See USPS, Fiscal Year 2006 Cost Segments and Components (Cost Segment 17).

Service in the NSA are offered in exchange for the discounts and other benefits: that is the nature of a multi-part contract. But that fact hardly warrants having the Commission, in balancing the value of what the Postal Service will give against what it will get, arbitrarily ignore much of the consideration that BAC has placed on the Postal Service's side of the scales. Order No. 1391, *supra*, 69 Fed. Reg. at 7577-78, 7580.

Equally without merit is Valpak's contention that the Commission should disregard the benefits to the Postal Service from having more than three billion pieces of BAC letter mail available as a large scale test of Intelligent Mail technology merely because this case has not been submitted for approval as an "experiment" under Rules 67 through 67d. Valpak Br. 19. Rules 67-67d offer an optional procedure for simplified review of certain rate and classification changes deemed to be experimental. Nothing in the Commission's rules, however, suggests that Rules 67-67d are the *exclusive* vehicles for consideration of experimental proposals, let alone that a proposed rate and classification change *must* be submitted for review under Rules 67-67d merely because the proposal has one or more elements that may be regarded as experimental.

To the contrary, the Commission declined to review the Capital One NSA case under the experimental rules despite its "extreme novelty." MC2002-2 PRC Op. & Rec. Decis. (May 15, 2003) ¶¶ 2014-2017 (citing Presiding Officer's Ruling No. MC2002-2/3 at 5); *id.* at ¶¶ 4001-4039 & App. C. Moreover, the Commission has not only approved but required, in the Capital One NSA and every subsequent NSA, the implementation of data collection plans aimed at gleaning

information from the NSA that might be of future use to the Postal Service and other mailers. “Such information could point the way to other creative opportunities for the Postal Service to raise new contribution and lower the costs of providing its services.” *Id.*, ¶ 9007; see also Order No. 1383, Docket No. RM2003-5, *Negotiated Service Agreements*, 68 Fed. Reg. 52546 (Sept. 4, 2003) at 52550 (col. 1) (discussing potential benefits of data collection plans). None of these pronouncements support the rigid dichotomy between short-term contribution maximization and longer-term R&D that Valpak would read into the Commission’s procedural rules for evaluating NSA proposals.

C. The Expiration Of The Postal Service’s Authority To File A Traditional Rate Case On December 20, 2007, Will Insulate Other Mailers From Even The Theoretical Possibility That The Loss Of Contribution From An NSA Could Result In Higher Rates On Other Services.

The NSA opponents’ challenge to the baseline values of the proposed discounts for mail processing performance suffers from a further, and even more fundamental, problem. Enactment of PAEA has eliminated the putative threat of harm to other mailers that the Commission relied on to justify oversight of NSA discount terms in the first place: the risk that the “burden of recovering” any loss in “contribution” resulting from unnecessary or needlessly large NSA discounts “would fall largely on captive monopoly mailers not party to the agreement.” BAC Br. 35-36.

PAEA has eliminated this risk by severing the link between the contribution from NSAs and the regulatory ceiling on other postal rates. Regardless of the profitability of any individual NSA, or even all NSAs in the

aggregate, 39 U.S.C. § 3622(d) caps overall increases to the levels justified by the CPI. 39 U.S.C. §§ 3622(d)(2)(A) , 3622(d)(1)(D). BAC Br. 21 (1st ¶), 36. If the Postal Service offers excessive or needless discounts to an NSA partner, the Postal Service alone will bear the financial consequences. BAC Br. 36.

The financial effect of the proposed NSA on the Postal Service will not be known until long after December 20, 2007, when the Postal Service's ability to seek rate increases under the pre-PAEA ratemaking standards lapses under 39 U.S.C. § 3622(f)). Thus, there is no possibility that the amount of financial contribution generated by the BAC NSA could influence the regulatory constraints on any future rate changes of general applicability. BAC Br. 22-23, 36-38.

OCA tries to brush off the implications of PAEA on the theory that the Commission's rules implementing PAEA are still "hypothetical" at this point. OCA Br. 2. There is nothing hypothetical, however, about the imminent expiration of the Postal Service's right to seek rate increases on the ground that its aggregate revenue fails to cover total attributable and institutional costs. That event occurs on December 20, 2007—little more than four months from today—by operation of law. 39 U.S.C. § 3622(f)). And OCA does not dispute that the economic impact of the NSA will not be known until well after that date.

D. Adjustments To The Baseline Read/Accept Rates Negotiated By BAC And The Postal Service Would Reduce The Economic Incentive For BAC To Invest In Improved Performance, And Could Jeopardize The Entire NSA.

Of the three participants that oppose the proposed NSA, only one—OCA—seeks to do so by imposing a “stop loss cap” on the discounts paid under the NSA. As noted above, OCA would limit the total discounts paid by the Postal Service over the three-year term of the NSA to “\$8,339,991”—ostensibly “the savings to the Postal Service from reduced forwarding and returns.” OCA Br. 9.

BAC and the Postal Service have previously explained why “stop loss caps,” adjustable baseline values, and other modifications to the NSA terms negotiated by the parties would be counterproductive. BAC Br. 41-43; USPS Br. 34-35; BAC Comments on Notice of Inquiry No. 1 (April 17, 2007) at 12, 18-23; BAC Reply Comments on Notice of Inquiry No. 1 (April 24, 2007) at 8-10. Among these proposals, however, the OCA proposal stands out for its sheer recklessness.

OCA’s proposal would cut the potential benefits to BAC from the NSA by two-thirds or even more. The bargained-for benefits that the OCA cap would confiscate from BAC would not be limited to discounts for improvements in mail processing performance. BAC also would receive no credit for benefits to the Postal Service that *do not depend on* improvements in read/accept rates, including the several million dollars annually that the Postal Service is likely to save from the barcoding of Courtesy Reply Mail and Business Reply Mail,³⁴ and

³⁴ See BAC Br. 12; Tr. 468, 479 (BAC discovery responses).

the \$3 million in estimated cost savings at the delivery unit from better address quality.³⁵

Indeed, the cap proposed by OCA could very well deprive BAC of a significant share of the benefits even from reducing forwarding and return rates. The NSA proponents' projections of \$8.3 million in savings from improvements in forwarding and return rates are "preliminary and highly approximate" "rough predictions" of how BAC's forwarding and return rates will improve in response to the NSA rate incentives.³⁶ If actual After Rates improvement were at the higher end of the range of projected After Rates outcomes, then the \$8.3 million cap would give the Postal Service a windfall from improved forwarding and return rates alone.

Needless to say, a discount "cap" as confiscatory as OCA's proposal would be effectively tantamount to rejection of the NSA outright. BAC is willing to invest in improving address quality and other mail attributes only to the extent that the anticipated incremental benefits over the three-year term of the NSA exceed the expected incremental cost. BAC Br. 42; USPS Br. 27, 34. The reduced stream of discounts allowed by the OCA proposal would not come close to covering the costs to BAC of performing under the NSA. BAC Br. 42-43; USPS Br. 34-35.

³⁵ The latter savings alone are conservatively projected to reach \$3 million. See Ayub Direct (USPS-T-1), App. A at 2, lines 7 and 8.

³⁶ Jones Direct (BAC-T-1) at 17; Tr. 132 (Ayub response to OCA/USPS-T1-31(a)).

Under the circumstances, the Capital One and Bank One NSA cases, which OCA invokes as authority for imposing discount caps here (OCA Br. 7), are instructive, although not in the sense contemplated by OCA. The fundamental impetus for the stop-loss cap in *Capital One* and its progeny appears to have been the Commission's belief that asymmetries in knowledge possessed by the Postal Service and its mailer co-proponent about the Before Rates volumes of the mailer could create a "moral hazard"—i.e., could enable the mailer to hoodwink the Postal Service by understating the mailer's anticipated Before Rates volumes. See, e.g., *Capital One NSA*, MC2002-2 PRC Op. & Rec. Decis. ¶ 5094. By contrast, the uncertainties over BAC's actual Before Rates read/accept rates are bilateral—i.e., shared by BAC as well as the Postal Service. The Postal Service's information about BAC's current mail processing performance is as good (or poor) as the information possessed by BAC itself. See Notice of Inquiry No. 1 (served April 3, 2007) at 1 ("The current Bank of America-specific read/accept rates are unknown by the Postal Service *and Bank of America.*") (emphasis added).

The history of the "stop loss" caps imposed in the prior volume incentive NSA cases is instructive in one important respect, however. It confirms that such a cap is likely to increase, not decrease, the financial risk facing the Postal Service by choking off large financial benefits the Service otherwise would have received from an uncapped NSA. As an executive for JPMorgan Chase testified about the financial effect of the stop loss cap imposed in the Bank One NSA case:

The rules adopted by the Commission to reduce the financial risk of NSAs to the Postal Service have also increased the risk that the potential financial benefits will never be fully realized. Our NSA is a good example of that situation. While we continue to abide by all of the mail preparation and other terms of the NSA, we reached the discount cap midway through the second year of our three-year NSA. When the rate incentives to use First-Class Mail were exhausted, First-Class Mail immediately became uneconomic for solicitations to many of our target markets, and many of our solicitation mail volumes have migrated back to Standard Class mail, depriving the Postal Service of several million dollars of additional contributions to institutional costs that the Service would have received if the NSA discounts had been uncapped.

Testimony of Daniel C. Emens, Vice President, J.P. Morgan Chase, during field hearing in Wilmington, Delaware, in Docket No. RM2007-1 (July 9, 2007), Tr. 27-28.

E. Implementation Of The Commission's Pricing Rules Under PAEA Will Render The Objections Of APWU, OCA And Valpak Moot By Allowing USPS To Implement This Or Any Other NSA On Only 45 Days Advance Notice – And With None Of The Costly And Intrusive Advance Review That BAC And The USPS Have Endured Here.

As BAC previously noted, the promulgation of Commission rules implementing 39 U.S.C. § 3622(c)(10) should render the objections of APWU, OCA and Valpak moot within the next few months. PAEA requires the Commission, in establishing a system for regulating rates for market-dominant products, to take into account “the desirability of special classifications for both postal users and the Postal Service . . . , including agreements between the Postal Service and postal users, when available on public and reasonable terms to similarly situated mailers.” *Id.* § 3622(c)(10). BAC Br. 21. Once the rules are in place, the Postal Service will be entitled to implement rate changes on 45

days' notice, including rate changes resulting from NSAs under Section 3622(c)(10). *Id.*, § 3622(d)(1)(C). BAC Br. 22.

The scope of Commission review of proposed rate changes during this 45-day period will be limited. As the Senate sponsors of the legislation recently stated, “The 45-day period that the Act gives the Commission to review [the] rate filing is largely intended to be used to determine whether or not a rate filing is within the rate cap.” BAC Br. 20-21 (Carper-Collins letter), 21 n. 5).

While APWU *et al.* in theory could file complaints against NSAs after they took effect, the substantive grounds for doing so will be limited. Nothing in Sections 3622(c) or (d)—or any other provision of PAEA—conditions the right to make selective rate reductions, or to establish discounts through NSAs, on a high level of certainty that the NSA will increase the contribution made by the affected mail to the Postal Service’s institutional costs. BAC Br. 22. To the contrary, an NSA that enhances the performance of mail processing and other Postal Service functions, as this would do, need not be contribution positive at all. An agreement that “enhance[s] the performance of mail preparation, processing, transportation, or other functions” is not required to increase the “overall contribution” of the mail “to the institutional costs of the Postal Service.” *Id.* § 3622(c)(10)(A). Under the circumstances, imposing regulatory constraints that will lose any legal basis within a few months would be irrational and wasteful.

The NSA opponents respond to these facts by ignoring them (APWU and Valpak) or by demanding that the Commission ignore them (OCA). See OCA Br. 1-2 (asserting that the consequences of the new law will remain “hypothetical”

until the Commission issues its implementing rules). The Commission, however, is presumably advanced enough in its work in RM2007-1 to have a better sense than any of the parties here about how its forthcoming rules will deal with NSAs. And the Commission has recognized that giving recognition to the likely contours of ratemaking under PAEA is entirely sensible when establishing rates under the old law. See R2006-1 PRC Op. & Rec. Decis. at iv (deferring to Postal Service judgment re pricing of competitive mail products in light of forthcoming changeover of regulatory authority to PAEA.). Like Dorothy in *The Wizard of Oz*, the Commission has no obligation to honor demands that the Commission figuratively “pay no attention to the man behind that curtain.” BAC Br. 38.

F. The Notion That The Commission Should Micro-Manage The Profitability Of This NSA Is Hopelessly At Odds With The Recognition By APWU *et al.* That PAEA Warrants A Hands-Off Approach To The Pricing Of Competitive Services.

APWU *et al.* also ignore the fundamental inconsistency here between the interventionist role they urge upon the Commission here and the laissez faire posture they ask the Commission to take regarding the pricing of other market dominant and competitive services. BAC Br. 39-41.

II. OTHER LEGAL CHALLENGES TO THE NSA ARE WITHOUT MERIT.

The handful of other arguments offered by APWU, OCA and Valpak against the NSA are also unfounded.

(1) For the reasons noted by BAC in their initial briefs, the proposed NSA would not discriminate unduly against competitors of BAC or otherwise

impair downstream competition. BAC Br. 43-46; USPS Br. 41-43. APWU's discrimination claim is merely a variant of APWU's generic position that the NSA would make the Postal Service financially worse off, and therefore would require higher rates of non-NSA mailers. APWU Br. 5. So is APWU's contention that the NSA would violate the "delinking" standards upheld by the Commission in R2006-1. *Id.* And so is Valpak's contention that the NSA could "result in aggregate workshare discounts exceeding 100 percent of avoided costs." Valpak Br. 10 & n. 9. All three claims founder on the evidence that the NSA as a whole would make the Postal Service better off.

(2) Valpak contends that paying BAC discounts for using Intelligent Mail Barcodes would be unfair after 2009, when the Postal Service currently plans to require the use of such barcodes. Timetables for generational shifts in technology, however, have a tendency to slip.³⁷ In any event, the use of Intelligent Mail Barcodes is only one of many operational changes that would be necessary conditions for BAC to qualify for discounts under the NSA. Finally, *none* of those operational changes would qualify BAC for discounts unless BAC

³⁷ Consider a more modest example: the reduction of the mandatory minimum Move Update cycle from 185 to 95 days, and the extension of Move Update requirements to Standard Mail. The Postal Proposed announced these changes in August 2003, with an effective date 18 months after the publication of a final rule. *Changes to the Move Update and Address Matching Requirements*, 68 Fed. Reg. 51750 (2003). In response to objections from mailers and vendors that these changes were premature, the Postal Service delayed issuing a follow-up notice starting the clock on the 18 month period until May 2007, almost four years after the first notice. *New Address Quality Standards for First-Class Mail and Standard Mail*, 72 Fed. Reg. 28908 (2007).

also achieves measurable improvements in its mail performance. Ayub Dir. (USPS-T-1) at 5 & 13; Tr. 254, 273, 297, 299 (Ayub discovery responses).

(3) Valpak speculates about where the Postal Service will draw the boundaries between arrangements with other mailers that are functionally equivalent, and arrangements that will not qualify as NSAs. Valpak Br. 17, 21. This issue is premature, however, and the Commission should decline to be drawn into it now. The Postal Service has made clear that it is interested in negotiating functionally equivalent NSAs with mailers who offer functionally equivalent terms and conditions—including mailers that already have made some of the operational changes required by the NSA. Tr. 373-74 (Ayub). Indeed, the Postal Service would be interested in negotiating with Valpak itself. See, e.g., Tr. 270 (Ayub). If Valpak is genuinely interested in pursuing a functionally equivalent NSA based on the present proposal, Valpak should test the Postal Service's *bona fides* by responding to this invitation. Absent such efforts, however, there is no live case or controversy for the Commission to resolve. And Valpak certainly has no standing to speak on behalf of other mailers who might be potential candidates for a functionally equivalent NSA—none of which have intervened in opposition to this NSA.

(4) Finally, Valpak renews its perennial campaign to replace NSAs with niche classifications. Valpak Br. 13-16. The Commission has consistently rejected such a position, however, absent a showing by the proponents of a niche classification that the mailer-specific terms in the proposed NSA were

unnecessary, or that other mailers that could satisfy those terms fully.³⁸ Valpak has made no such showing. To the contrary, the record demonstrates that the mail profiles and circumstances of individual mailers are likely to vary too much to offer terms identical to this NSA to multiple mailers through a niche classification. USPS Br. 38-40 (citing record); see also Tr. 279 (Ayub response to VP/USPS-T1-18(d)). Valpak of all parties should agree. One of the most likely consequences to a shift from NSAs to niche classifications would be an increased reliance on system-average data for baseline values—the very thing that Valpak and its allies decry in this proceeding.³⁹

³⁸ *Capital One NSA*, MC2002-2 PRC Op. & Rec. Decis. (May 15, 2003) ¶¶ 3039-3040; Order No. 1391, Docket No. RM2003-5, *Negotiated Service Agreements*, 69 Fed. Reg. 7574, 7578 (2004); *Bookspan NSA*, MC2005-3 PRC Op. & Rec. Decis. (May 10, 2006) ¶¶ 4016-4018.

³⁹ Moreover, the most practical way to determine whether an arrangement similar to the proposed NSA could be established as a niche classification would be to allow the Postal Service to gain experience by implementing this NSA and several functionally equivalent NSAs based on it. See Tr. 268-269 (Ayub response to VP/USPS-T1-15). But the Postal Service is unlikely to gain such experience as long as entities with no real financial stake in a proposed NSA are permitted to intervene and interpose costly and time-consuming procedural and substantive barriers to its implementation.

CONCLUSION

For the foregoing reasons, Bank of America Corporation respectfully requests that the Commission recommend the Negotiated Service Agreement without modification. BAC also requests that the Commission issue its decision as expeditiously as the record, and the Commission's docket, permit.

Respectfully submitted,

Stacey Stone Bennett
Assistant General Counsel
Global Staff Support Functions
BANK OF AMERICA, N.A.
101 South Tryon Street
NC1-002-29-01
Charlotte, NC 28255
(704) 388-6583
stacey.stone_bennett@bankofamerica.com

David M. Levy
Richard E. Young
SIDLEY AUSTIN LLP
1501 K Street, N.W.
Washington, DC 20005-1401
(202) 736-8000
dlevy@sidley.com
ryoung@sidley.com

Counsel for Bank of America Corporation

August 13, 2007
Refiled August 14, 2007