

**BEFORE THE POSTAL REGULATORY COMMISSION  
WASHINGTON, DC 20268-0001**

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**Review of Nonpostal Services**

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**Docket No. MC2008-1(Phase II)**

**REPLY BRIEF OF PITNEY BOWES INC.**

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## **I. INTRODUCTION**

Pitney Bowes submits this brief in reply to points raised in the initial briefs of the Public Representative and the Postal Service. Some of the issues raised have been resolved earlier in this 19-month-long proceeding, some of the issues remain to be resolved in the current phase of the proceeding, and some of the issues will likely need to be decided by the Court of Appeals. Finally, this reply brief summarizes where matters stand on the authority of the Postal Service to enter into new services, and what remains to be decided with respect to its ability to do so going forward.

The initial briefs and the record evidence in this proceeding establish that the licensing arrangement for USPS-branded replacement postage meter ink cartridges (USPS-branded ink) should not be approved as a grandfathered nonpostal service because: (1) the private sector is meeting the public need for postage meter supplies under Section 404(c)(3), and (2) USPS-branded ink was not “offered” as of January 1, 2006 as required by section 404(e)(2).

The arguments to the contrary offered by the Postal Service are unsupported on the record and inconsistent with the language, structure and intent of the PAEA. The Postal Service’s contention that the Commission has approved the “general conduct” of licensing without regard to the manifestation of any future licensing activity is unsupportable. This over-broad interpretation subverts the transparency and accountability objectives of the PAEA and eviscerates the Commission’s oversight responsibilities. Accordingly, the Commission should determine that USPS-branded ink may not continue as a grandfathered nonpostal service and direct the Postal Service to terminate the offering pursuant to section 404(e)(4).

The following findings have been established for purposes of this proceeding:

- The Commission, not the Postal Service, determines what activities constitute services;
- A “service” is (1) an ongoing activity, (2) of a commercial nature, (3) offered to the public, (4) for purposes of financial gain;
- Only two types of services are provided by the Postal Service: those that are postal services and those that are “grandfathered” nonpostal services;
- The Commission determines what is “postal” and what is “nonpostal”;
- The Commission regulates all postal and all grandfathered nonpostal services;
- The Postal Service cannot offer new postal services without consideration by and approval of the Commission; and
- The Postal Service is barred from offering any new nongrandfathered nonpostal service.

What remains to be determined is whether the Postal Service may *indirectly* engage in *new* nonpostal services via licensing arrangements, and if so, whether it may do so without approval or regulation by the Commission. Throughout the course of these proceedings, numerous parties have argued that such new arrangements are not permitted under the PAEA.<sup>1</sup> To the extent the Commission permits the Postal Service to offer new nonpostal licensing arrangements or variations of preexisting licensing arrangements, the Commission must exercise vigorous regulatory oversight. Vigorous review and oversight is particularly important for consumer protection where the Postal Service is engaged in branding activities related to postal operations and to protect against unfair competition where the Postal Service is offering licensed products in commercial markets over which it exercises regulatory authority. The specific scope

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<sup>1</sup> See Pitney Bowes Inc. Comments on United States Postal Service Response to Order No. 126, November 24, 2008, at 15-16; Schiff Hardin Letter on Behalf of Francotyp-Postalia, Inc. to Chairman Blair, dated November 24, 2008, at 1-2; Comments of Association of Postal Commerce, Alliance of Nonprofit Mailers, Direct Marketing Association, National Postal Policy Council and Parcel Shippers Association on Licensing Agreements, November 24, 2008, at 2; Initial Brief of Pitney Bowes, Inc. (Phase II), July 21, 2009, at 9-10; Initial Brief of the Public Representative (Phase II), July 21, 2009, at 6.

and nature of this review is an issue that is appropriately deferred to the future proceeding (Phase III) that the Commission intends to establish to develop regulations applicable to authorized nonpostal services. *See* Order No. 168, at 1, n.2.

## II. OVERVIEW

Below Pitney Bowes provides its overview and summarizes where matters stand in this proceeding, and what must be done to correctly implement the commands of the PAEA.

Under the PAEA, the Commission, not the Postal Service, is vested with the authority to determine which offerings are “nonpostal services” within the scope of section 404(e) and which of those offerings should continue. Early in this proceeding the Postal Service argued that it could unilaterally withhold certain nonpostal services from the Commission’s review. *See e.g.*, Initial Brief of the United States Postal Service, September 10, 2008. The Commission has repeatedly rejected this view.<sup>2</sup> Pitney Bowes and other participants have agreed with the Commission on this issue. The Postal Service appealed this issue to the Court of Appeals where it is now pending.<sup>3</sup>

The Commission has defined a service as “(1) an ongoing activity, (2) of a commercial nature, (3) offered to the public, (4) for purposes of financial gain,” and pointed out, importantly, “[i]n this context, financial gain encompasses remuneration established by or with the agreement

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<sup>2</sup> *See* Order No. 74, at 10 (“the Postal Service Response does not cure that failure because it is predicated on the unsustainable theory that the Postal Service, not the Commission, is authorized to determine which services, that are *not* postal services, offered by the Postal Service on December 20, 2006 constitute nonpostal services that, under the PAEA, are subject to the Commission’s authority to terminate or continue.”) Order No. 154 at 26 (“The PAEA eliminated the Postal Service’s authority to provide new nonpostal services. It also defined the two types of services the Postal Service could lawfully provide. With that as the framework, 39 U.S.C. § 404(e) directs the Commission to review each grandfathered nonpostal service and determine which, if any, should continue. To be meaningful, that review must take into account all commercial, nonpostal services regardless of whatever putative authority the Postal Service may claim for offering them. Otherwise, the very activities that Congress sought to curb by rescinding the Postal Service’s authority to engage in new commercial, nonpostal ventures may be perpetuated. In sum, the Postal Service’s restrictive interpretation of 39 U.S.C. § 404(e) is unpersuasive.”).

<sup>3</sup> *See United States Postal Service v. Postal Regulatory Commission*, Case No. 09-1032 (D.C. Cir)(filed January 16, 2008).

of the Postal Service.” Order No. 154, at 2. The Commission has further noted that “[t]hus, by definition, only two types of services are provided by the Postal Service: those that are postal services and those that are nonpostal services.” *Id.*

The Postal Service may offer new postal services only if approved by the Commission under section 3642. *See* 39 U.S.C. § 3642. With respect to nonpostal services, section 404(e)(3) requires the Commission to “review each nonpostal service offered by the Postal Service . . . and determine whether that nonpostal service shall continue.” 39 U.S.C. § 404(e)(3). Section 404(e)(2) limits the Postal Service’s authority to provide nonpostal services to those it “offered as of January 1, 2006.” The purpose of the Commission’s review under section 404(e)(3) is to determine which nonpostal services should continue, taking into account the public need for the service and the private sector’s ability to meet that public need. Thus, the Postal Service is generally prohibited from offering new nonpostal services. The law here is amply supported by the legislative history.<sup>4</sup>

Defining the scope of permissible licensing activities has complicated what once appeared to be a rather straightforward exercise under section 404(e). The Commission has attempted to interpret the strictures of section 404(e) in a manner that does not unduly constrain the Postal Service’s ability to continue preexisting licensing activities. In Order No. 154, however, the Commission appears to have left open the possibility that the Postal Service could offer new licensing agreements *unrelated* to those it offered as of January 1, 2006. *See* Order No. 154, at 73. The Postal Service has seized on this aspect of Order No. 154 to push for an

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<sup>4</sup> *See* Order No. 154 at 16-22; Pitney Bowes Inc. Comments on United States Postal Service Response to Order No. 126 Regarding Licensing Agreements, Appendix A (November 24, 2008).

even more expansive interpretation that would allow it to engage in a limitless range of future licensing activities without any provision for the review or approval by the Commission.

As the Public Representative argues in its most recent submission – and as numerous other parties throughout the course of this proceeding have likewise argued – this result is inconsistent with the language, structure and intent of the PAEA. *See* n.1, *supra*. The Postal Service’s position would lead to the illogical result that legislation intended to (1) confine the Postal Service to its core “postal” activities and (2) strengthen the regulatory oversight and accountability of those postal activities could be read to provide the Postal Service with unfettered, unregulated authority to do indirectly, through licensing or leasing, that which it could not do directly.

The Commission has previously held that “[u]nder the PAEA, the Postal Service is not free to offer, under the guise of separate statutory authority, essentially the same commercial nonpostal services which Congress curtailed in 39 U.S.C. 404(e).” Order No. 154 at 10. This applies with equal force to the new nonpostal licensing activities of the Postal Service.

Accordingly, the Commission should reconsider its interim holding in Order No. 154 to allow the Postal Service unfettered authority to engage in new nonpostal licensing activities. The Public Representative has advocated in favor of imposing the limitations of section 404(e)(2) on a license-by-license basis. *See* Initial Brief of Public Representative, at 6. Alternatively, Pitney Bowes advocates in favor of limiting future licensing activities to those that are nonsubstantive variations to the licensing activities offered by the Postal Service as of January 1, 2006. Either approach is superior to the Commission’s interim position, interpreted by the Postal Service as the unfettered authority to do indirectly, through a limitless range of licensing activities, that which the PAEA prevents it from doing directly.

Moreover, to the extent the Commission allows the Postal Service to introduce new licensing arrangements or variations of preexisting licensing activities, the Commission must exercise regulatory oversight.<sup>5</sup> Vigorous review and oversight is particularly important for consumer protection where the Postal Service is engaged in branding activities related to postal operations and to protect against unfair competition where the Postal Service is offering licensed products in commercial markets over which it exercises regulatory authority. The scope and nature of the Commission’s review of such licensing activities is an issue that is appropriately deferred to the future proceeding (Phase III) that the Commission intends to establish to develop regulations applicable to authorized nonpostal services. *See* Order No. 168, at 1, n.2.

### **III. ARGUMENT**

#### **A. There Is No Public Need for USPS-Branded Ink**

The Postal Service miscasts the public need analysis by shifting the focus to its own revenue generating needs. The statutory framework and legislative intent of the PAEA make clear that this is not correct. The proper focus is on the consumer’s need for a particular product.

The Postal Service has offered no evidence that there is a public need for USPS-branded ink. Nor does the Postal Service’s initial brief even attempt to argue any particularized showing of public need that is specific to USPS-branded ink. Rather, the Postal Service contends that licensing in general serves a public need because it generates revenue that makes a contribution to institutional costs and because licensing promotes the Postal Service brand. *See* USPS Initial

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<sup>5</sup> “Absent notice and review, new commercial licensing agreements – however dissimilar in nature from the licensing agreements previously reviewed by the Commission – will exist outside the control of the Commission; a *de facto* ‘third bucket.’ As a practical matter, this would allow the Postal Service to do indirectly that which it cannot do directly – offer new revenue-generating activities that are not approved postal or grandfathered nonpostal services. This is inconsistent with the PAEA’s fundamental commitment to transparency and accountability.” Pitney Bowes Initial Brief at 11.

Brief, at 10. But generating revenue and promoting the brand serve the Postal Service's needs, not the public need. Any public benefit is indirect and incidental. As discussed in Pitney Bowes' previous submissions, the "needed revenue" rationale alone cannot be sufficient. By definition, all nonpostal services subject to grandfather approval are revenue-generating activities. *See* Order No. 154, at 2. To accept the "needed revenue" argument advanced by the Postal Service here would render the public need test in section 404(e)(3)(A) mere surplusage.

The Postal Service also reiterates the general argument that licensing activities increase the Postal Service's visibility and, therefore, promote the use of the mails. *See* USPS Initial Brief at 10-11. But the appeal to the promotional benefits of licensing is of no help in the context of USPS-branded ink. First, the object of USPS-branded ink is *not* to promote the Postal Service's brand or the use of the mails; it is to promote a commercial product. Second, the promotional value of USPS-branded ink cartridge is trivial – when in use the cartridge is concealed in the postage meter – and consumers purchasing replacement meter ink cartridges are already committed to the use of the mails.

With respect to USPS-branded ink the unfair advantage compared to others is high, the promotional value is negligible, and the risk for consumer confusion is high. The Public Representative correctly observes that consumers purchasing USPS-branded promotional merchandise (*e.g.*, a T-shirt or coffee mug) are unlikely to perceive that the quality of the product is somehow enhanced by the USPS-brand. *See* Public Representative Initial Brief at 2. In contrast, consumers purchasing a USPS-branded item that relates to postal operations may well perceive that the quality of the product is enhanced because it appears to be an "official" product. *See id.*, at 3, 5; Pitney Bowes Response to POIR No. 2, June 24, 2009, Question 6. Consumers

would inherently believe that since the Postal Service is accepting the mail for delivery that using USPS-brand ink would be the best course of action to ensure proper handling of the mail.

Moreover, the use of the Postal Service brand in a commercial context related to postal operations has the potential to mislead and confuse consumers and the mailing public. Of course, this is what the Postal Service wants: “consumers will now have the option to acquire meter ink while maintaining the brand connection with the trusted provider of delivery for metered mail; this may prove to be particularly attractive to consumers.” USPS Initial Brief at 17. The problem, however, is that the brand connection is an illusion. In reality, USPS-branded ink is the very same product that was previously available to consumers under a private label. The underlying products are identical, nothing has changed except for the packaging.

The potential for public confusion or deception is a serious issue that undermines the Postal Service’s contention regarding the “basic appropriateness” of the use of the USPS-brand on commercial products related to postal operations. In fact, the opposite is true; licensing activities for commercial products related to postal operations ought to be subject to greater scrutiny to ensure that consumers are not misled or deceived.

Finally, the argument that USPS-branded ink will increase access to the mails or enhance the convenience of the mailing public also is without merit. *See* USPS Initial Brief at 10. The Postal Service has offered no evidence that USPS-branded ink is being made available through new or expanded retail channels. To the contrary, the record evidence establishes that access to postage meter supplies is plentiful and that the Postal Service has merely rebranded and repackaged an existing commercial product and is using the very same retail channels used by existing private sector competitors. *See* Declaration of Peter Wragg (Wragg Decl.), May 11, 2009, at ¶ 16, Ex. 1. Therefore, the public need for access and convenience recognized by the

Commission in other contexts (*e.g.*, photocopying services or passport photo services), *see* Order No. 154 at 41-44, is absent in the case of USPS-branded ink. USPS-branded ink does not expand consumer access to the mails, it merely displaces the services *already* provided by private sector competitors.

For all of these reasons the Postal Service has failed to establish a public need for USPS-branded ink.

**B. The Private Sector Is Meeting the Public Need for Postage Meter Supplies**

The Postal Service asserts, without more, that the “record evidence belies” the assertion that the private sector is meeting the public need for postage meter supplies. But the Postal Service does not cite to any evidence to support this claim because there is none. In contrast, Pitney Bowes has submitted evidence establishing that consumers looking to purchase postage meter ink may do so via national, household-name retailers (*e.g.*, Kmart, Office Depot, Walgreens, Staples, Office Max, etc.) or via hundreds of on-line retail websites, including eBay, Amazon.com, Yahoo.Shopping.com, and many, many others. *See* Declaration of Peter Wragg (Wragg Decl.), May 11, 2009, at ¶ 16, Ex. 1. Pitney Bowes has also introduced evidence establishing the presence of dozens of private label manufacturers, not just Pitney Bowes, Hasler, Neopost and other original equipment manufacturers (OEMs), *all* of whom would be forced to compete with USPS-branded ink. *See id.*

The Postal Service does not and cannot dispute that there are many, many third party suppliers competing in the meter supplies market or that postage meter ink is available through a variety of retail sales channels. *See* USPS Initial Brief at 16. Nevertheless the Postal Service relies uncritically on the unsupported allegations raised by Pinpoint LLC to suggest that USPS-branded ink is necessary as an alternative for “replacement cartridges other than those produced

by the OEM.” *Id.*, at 17. But the record is clear that there are already numerous different replacement ink cartridges available from a great number of third-party suppliers in competition with the OEMs. *See* Wragg Decl., at ¶ 16, Ex. 1. Thus, there is no public need for USPS-branded ink because the private sector is already meeting the public need for postage meter supplies.<sup>6</sup>

Finally, as Pitney Bowes has previously explained, there are reasons for the PRC to be even more vigilant in its review of nonpostal services where the Postal Service seeks to compete in markets in which it also exercises regulatory authority. *See* USPS Brief at 13-16. The conflict of interest extends beyond the Postal Service’s “limited” regulatory authority over meter ink to the Postal Service substantial regulatory authority to approve new postage evidencing systems. *See* Lord Decl., at 1-2. Thus, a heightened degree of Commission scrutiny is important where, as here, the Postal Service’s participation as a competitor in commercial markets that it regulates will also create the potential for unfair competition that simply do not exist with other market competitors.<sup>7</sup>

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<sup>6</sup> The Postal Service’s argument that the potential classification of a grandfathered nonpostal service as a “competitive product” is relevant for purposes of the Commission’s consideration under section 404(e)(3) misses the mark. *See* USPS Initial Brief at 12. The undisputed record evidence concerning the maturity and competitive nature of the postage meter supplies market speaks to the fact that the private sector is meeting the public need for postage meter supplies. The potential classification of an approved nonpostal service under section 404(e)(5) has no bearing on the initial finding under section 404(e)(3)(B). A nonpostal service is subject to classification and regulation as a “market dominant” or “competitive” product under section 404(e)(5) *if and only if* it has been approved under section 404(e)(3). The relevant question under the PAEA is not one of “competition policy,” but rather the ability of the private sector to meet the public need for the nonpostal service the Postal Service is seeking to offer. With respect to USPS-branded ink, the Postal Service has failed to establish a public need for this service and the evidence before the Commission established that the private sector is fully meeting the public need for postage meter supplies.

<sup>7</sup> The unique competition issues are that the Postal Service has: (1) access to Pitney Bowes’ new product designs prior to product launch; (2) a financial incentive to delay approval of Pitney Bowes new products to foster continued sale of USPS-branded ink cartridges for use in legacy Pitney Bowes products; and (3) access to Pitney Bowes’ proprietary customer information.

Accordingly, the Commission should not grandfather USPS-branded ink to continue because the record conclusively establishes that the private sector is meeting the public need for postage meter supplies.

**C. USPS-Branded Ink Is Not Eligible for Grandfather Approval Because It Was Not “Offered” as of January 1, 2006**

The PAEA limits the range of permissible nonpostal services to those that were “offered as of January 1, 2006” and approved by the Commission. 39 U.S.C. § 404(e)(2). USPS-branded ink is not eligible to be grandfathered as a nonpostal service under section 404(e)(2) because it was not offered as of January 1, 2006. *See* USPS Response to Order No. 126, Attachment at 1; PRC Order No. 171, at 5, n.6.

The Postal Service discusses at length its interpretation of the scope of the Commission’s determination in Order No. 154 regarding grandfathered licensing activities. *See* USPS Initial Brief at 5-8. The Postal Service contends that the Commission has approved the “general conduct” of licensing without regard to the manifestation of any future licensing activity. *See id.* Under the Postal Service’s interpretation, the Commission has authorized the Postal Service to engage in a virtually limitless range of new nonpostal activities via licensing arrangements that it would be prohibited from providing directly. This view is unsupportable. Such an expansive interpretation would subvert the transparency and accountability objectives of the PAEA and negate the Commission’s oversight responsibilities. The Commission ought to reject the Postal Service’s overbroad interpretation in favor of a more limited determination required by the language and intent of the PAEA.

The Public Representative urges the Commission to assess each license under the eight-step process set out in Order No. 154. *See* Public Representative Initial Brief at 6. Under the

Public Representative's approach USPS-branded ink fails because it was not being offered as of January 1, 2006. *See id.*

Pitney Bowes recommends the Commission adopt an intermediate position; limiting new revenue-generating licensing activities to those products which are functionally equivalent to the licensing activities offered by the Postal Service as of January 1, 2006. For example, the Commission's approval of USPS-branded apparel (*e.g.*, logo T-shirts) or novelty logo merchandise (*e.g.*, logo coffee mugs) would encompass like products and logical outgrowths of those activities (*e.g.*, logo hats and logo travel coffee cups). This approach is consistent with the language and structure of section 404(e) and satisfies the Postal Service's practical concerns regarding the introduction of future licenses.<sup>8</sup> *See* USPS Initial Brief at 9. Accordingly, the Commission should reconsider and clarify its determination regarding the scope of eligible licensing activities.

**D. The Commission Should Develop a Framework for the Review and Approval of Future Licensing Activities**

Pitney Bowes concurs with the Public Representative that the Commission must develop a framework to ensure that future commercial licensing arrangements are subject to review and approval. *See* Initial Brief of Public Representative at 7. As the Public Representative observes, the procedures for notice and review, and the opportunity for interested parties to be heard on new commercial licensing arrangements will necessarily include categorization issues. *See id.* Importantly, the determination of how future licenses may be categorized is a determination reserved to the Commission.

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<sup>8</sup> Importantly, however, USPS-branded ink fails even under this test because it is materially distinguishable from the licensing activities offered by the Postal Service as of January 1, 2006.

The Public Representative has suggested that the Commission require pre-implementation review of any future licensing arrangement similar to the review provisions for contract rates not of general applicability. *See id.* (citing 39 C.F.R. §§ 3015, 3020). Pitney Bowes suggests the Commission consider a notice requirement with opportunity for public comment, in lieu of a pre-approval procedure. A simple notice provision would allow the Postal Service greater flexibility to bring new licensing arrangements to market, while satisfying the Public Representative's concern regarding public notice and the opportunity for interested parties to be heard.

Pitney Bowes anticipates that the follow-on proceeding regarding the scope and nature of the regulation of approved nonpostal services (Phase III) will provide an opportunity to address these important issues. *See* PRC Order No. 168, at 1, n.2.

#### **IV. CONCLUSION**

For the foregoing reasons, and those stated in the previous submissions of Pitney Bowes, the Commission should not approve USPS-branded ink as a grandfathered nonpostal service under section 404(e) because the private sector is meeting the public need for postage meter supplies. Moreover, even if the Postal Service could satisfy the public need test of section 404(e), USPS-branded ink is ineligible for approval as a grandfathered nonpostal service because it was not "offered" as of January 1, 2006, as required by section 404(e)(2).

