Postal Regulatory Commission
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BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

Exigent Request, 2010	)	Docket No. R2010-4

Comments of Discover Financial Service
August 17, 2010

Discover Financial Services (DFS) is pleased to submit these Comments in response to Order 485, released July 8, 2010, setting August 17, 2010 as the due date for Comments in this matter and September 2, 2010 as the due date for Reply Comments.

DFS is a financial services company that offers credit card services and other financial service products under the Discover® Card and Discover® brands. DFS is one of the largest First-Class and Standard Mail letter mailers in the United States, and has won awards for its quality, creativity, and dedication to the postal channel.

I. The Scope of This Proceeding.

In terms of the Scope of this proceeding, DFS believes that the multi-prong standard contained in Section 3622(d)(1)(E) of the Postal Accountability and Enhancement Act (PAEA), 39 U.S.C. §3622(d)(1)(E), should be implemented in a straightforward fashion. Under this Section, the Commission having a duty to determine:

1) Whether extraordinary or exceptional circumstances exist sufficient to justify an increase above the rate cap, and if so, then

2) Is the rate increases proposed by the Postal Service reasonable, equitable, and necessary, in order

> 3) To enable the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States, provided that the Postal Service.

Consequently, DFS would urge the Commission to restrict its decision in this proceeding to issues directly related to the three prongs, and not delve into other matters. Should a mailer wish to contest other matters, there is always the complaint process and the annual compliance determination process.

In terms of addressing the specifics of these issues, DFS will not challenge the Postal Service's filing on either the first or third prongs, given the fact that that we are in the midst of a series economic downturn and that the Postal Service has cut more than $6 Billion from its cost base in FY 2009

However, DFS would urge the Commission—should it find that extraordinary and exceptional circumstances do indeed exist —to strongly reaffirm that its expectations are that the Postal Service shall live within the price cap in the future not only under "normal" circumstances, but also under the more "difficult" economic circumstances that could prevail in the short term. Indeed, DFS would urge the Commission to ensure that the Postal Service understands that Section 3622(d)(1)(E) requests are to be the exception and not the rule.

As to the question of whether the proposed rates are reasonable equitable and necessary in the current circumstances, DFS is concerned that the Postal Service's proposed rate increase for Bulk First Class Letter Mail[1]—which is about six percent—is

[1] Bulk First Class letter/postcard mail is the term correctly used in the official Mail Classification Schedule to describe the category of First Class mail that DFS uses. It is contrasted to Single Piece Letters/Postcards, Flats, Parcels, and two types of International Mail. The Mail Classification Schedule is

pushing beyond the limit of reasonable, equitable, and necessary and would urge the Commission to consider reducing it back to the average.

DFS is more concerned, however, that the Commission might be tempted to unilaterally adjust this rate increase even higher out of a misguided assumption that it has a duty to do so under the worksharing provisions of the PAEA. Nothing could be further from the truth for First Class Bulk Letter Mail is a separate product, needs to be priced that way, and in fact, its relationship to single Piece First Class Mail ceased to be one of worksharing decades ago.

II. First Class Bulk Letter Mail Rates.

The cost per piece to deliver Single Piece First Class Letter Mail is 26.326 cents per piece.[2] The cost per piece to deliver Bulk First Class Letter Mail is 11.981 cents per piece.[3] That is a cost difference of 14.35 cents per piece. That means that Single Piece First Class Mail is *more than twice as expensive* to deliver as Bulk First Class Letter Mail.

The price of the Single Piece First Class Stamp is 44 cents. The price per piece of Bulk First Class Mail for a typical mailer is approximately 37 cents per piece.[4] That is a price difference of roughly 7 cents per piece, in contrast to the cost difference of 14.35 cents per piece. That is a huge discrepancy.

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set forth at Appendix A to Subpart A of Part 2020 and the latest version was adopted by the PRC at 75 Fed. Reg. 44138 (July 28, 2010).

[2] Postal Regulatory Commission's (PRC) 2009 Annual Compliance Determination at 67.

[3] Id.

[4] This can vary. This 37 cent figure is roughly what DFS pays for the average First Class Bulk Letter Mail piece and we understand that other bulk mailers prices are in the same ball park due to their mix.

If one does the math, one finds that the Postal Service makes 25 cents per piece from a typical Bulk First Class Letter Mail piece while it only makes 18 cents from a typical Single Piece First Class Letter Mail piece. In other words, the Postal Service makes a greater profit from a typical Bulk First Class Letter Mail than it does from a typical Single Piece Letter Mail. It thus logically follows that allegations that the Postal Service is giving a "special" deal and special discounts to Bulk First Class mailers—as compared to Single Piece First Class mailers—are groundless. Bulk Fist Class Letter Mail is *much cheaper* to deliver than Single Piece First Class Mail and it is only "just and reasonable" for bulk rates to reflect their much cheaper cost base. See U.S.C. § 3622(b)(8).

Indeed, since the price difference between Bulk and Single Piece First Class Letter Mail (seven cents) is *less than half the total cost difference* (14.35 cents), it seems that it is the Single Piece mailer that is currently getting the special deal, and not the Bulk mailer. This makes the Postal Service's decision to increase the price on Bulk First Class Mail by a greater percentage than Single Piece First Class Mail all the more difficult to comprehend.

There have been suggestions that the Commission should ignore the total cost differences between the two and only focus on the narrower subset of total costs known as "avoided costs" in setting rates. See e.g., Proposed Question 4 of the NALC, filed on August 5, 2010 in this docket. Indeed that was the approach that the Postal Service used before reliable cost data on Bulk First Class Mail was developed.

However, this is an approach that the Postal Service gave up a number of years ago, in recognition of the fact that the marketplace had evolved, and that such an

approach was no longer consistent with the reality of that evolved marketplace. As Witness Kiefer has stated, traditional workshare theory suggests that increasing presort First-Class Mail prices would simple cause customers to re-evaluate their decision to perform worksharing activities and if it cost more to presort mail than was available under the postal discount, then customers would simply choose to tender unsorted mail to the Postal Service. See Kiefer at 18.

Such a theory is based on the notion that 1) the Postal Service is a monopoly and that 2) the economics of their businesses would permit Bulk First Class Mailers to simply revert to Single Piece First Class Mail for their Statements if Bulk First Class Mail rates increase precipitously. This is not true.

The economics of the businesses of most Bulk First Class mailers are so tight that any increase in Bulk First Class rates is going to precipitate electronic diversion, and a significant increase is going to precipitate significant diversion. The greater the increase, the greater the diversion. In essence were Bulk First Class Letter Mail to increase significantly, the increase in electronic diversion would be substantial and little would flow back to Single Piece . Thus, taking the Bulk First Class Letter Mail increase up to nine or ten percent would have a serious impact on Bulk First Class Mail revenues as mailers would leave the system as quickly as they could and to the maximum degree that they could. It is a very serious matter. The Postal Service understands this, as Kiefer has testified. See Kiefer at 16-19.

DFS would like to assure the Commission that the Postal Service's view on this matter is exactly on point. While DFS has a fairly aggressive program in place to move statement mail to electronics, any significant increase in Bulk First Class Mail rates

would create enormous incentives to significantly speed up that program and effectively force DFS to do everything it could to remove as much as possible of its Statement Mail and other First Class Bulk Letter Mail out of the mail.

It took a long time for the Postal Service to finally understand and acknowledge how the marketplace has evolved and to realize that the theory of “reversion” of Bulk Mail to Single Piece Mail is no longer supported by the facts. DFS and others in the financial services industry have discussed this time and time again with the Postal Service. We are pleased that the Postal Service has finally come to understand that and urge the Commission to do so as well. It needs to do so for the health of the postal system, and in order to let the Postal Service manage First Class Bulk Letter Mail prices.

Several questions have been raised by Commissioners during the course of the hearings in this docket about the reliability of traditional elasticity data. Those questions are well placed. Even before the recession, because of the dynamic nature of the changing market, elasticity data looking backwards two or three years was not an adequate predicator of future action. This is even more true now, in this time of great recession. While the Postal Service has used old elasticity data in its deliberations, it has also taken a qualitative approach to the issue, and developed its business knowledge and business judgement and made decisions based on that knowledge base. Should the Commission try to second-guess that business judgement, based on simply mechanical and qualitative results of manipulating traditional elasticity data, the results could be disastrous. We urge it not to do so. Elasticity data in a dynamic market in the best of times is only so reliable. In the worst of times, it is even less reliable.

The best one can do is to intensely question the Postal Service about its decision making progress, look at the qualitative estimates that it has made, and see whether the results are consistent with those estimates. That is the way businesses work, and that is the way the Postal Service should work.

Thank you for considering our views.

Respectfully submitted,

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