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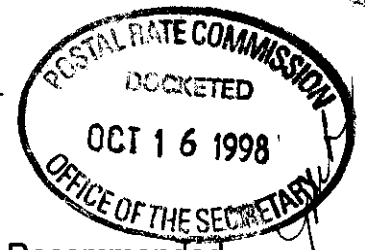
Before Commissioners: Edward J. Gleiman, Chairman;
W.H. "Trey" LeBlanc III, Vice Chairman;
Ruth Y. Goldway and George A. Omas

Mailing Online Service

Docket No. MC98-1

NOTICE OF INQUIRY NO. 1 CONCERNING
PROPOSED MAILING ONLINE EXPERIMENT

(October 16, 1998)



On October 7, 1998, the Commission issued its Opinion and Recommended Decision concluding the market test phase of Docket No. MC98-1. In its Opinion, the Commission identified several issues that it expected to be more fully developed during consideration of the proposed experiment phase of Mailing Online. Participants are requested to comment on these issues, which are summarized below.

Because of the need to expedite consideration of the proposed Mailing Online experiment, the Commission is asking parties to file their responses to the issues raised in this Notice at a time, and in a form, that will make it feasible to treat the fact-based portions of their responses as testimony. Accordingly, the Postal Service's responses to this Notice will be due 21 days from the date of this Notice. The Postal Service is invited to file appropriate portions of its responses as supplements to the direct testimony that it initially filed in this docket in support of its proposed Mailing Online experiment. This will afford other parties an opportunity to conduct oral cross-examination of the Postal Service's responses at the time that they cross-examine the testimony that the Postal Service initially filed in support of its proposed experiment. Other participants are invited to file any responses that they have on the issues raised

in this Notice at the time that they file their direct cases concerning the proposed experiment. If the Postal Service or other participants wish to have portions of their responses included in the record, they should be attested to by a witness who is prepared to stand cross-examination on them.

Issue No. 1.

For the market test, the Postal Service requested that it be allowed to charge what it considered to be a proxy for averaged postage rates for Mailing Online mailings (automation basic postage rates for all Mailing Online mailings, and destination BMC discounts to all Standard A Mailing Online mailings). To implement that request, the Postal Service sought approval of a waiver of the threshold volume requirements to qualify Mailing Online mailings for automation basic discounts. It also sought a waiver of the destination BMC entry requirements for the DBMC discount. The Postal Service chose not to apply deeper discounts to Mailing Online mailings for which they might otherwise qualify.

The Commission approved the requested waiver of eligibility requirements for the automation basic rate for the market test only. In doing so, it indicated that there is a need for further inquiry during consideration of the experiment concerning the need to apply automation basic postage rates to Mailing Online and the effects of waiving the minimum volume eligibility requirement on competition. The Commission indicated that the record should be further developed as to the specific nature of the transactional or business need for this waiver. PRC Op. MC98-1 at 27.

With respect to the effects of the waiver on competitors, the Commission indicated that the record should be further developed concerning what the relevant market is for Mailing Online, and the harm that competitors are likely to sustain. *Id.* at 26-27. In supplementing the record concerning the justification for, and the competitive effects of, the requested waiver, participants are requested to discuss the importance of the volume of Mailing Online mail that is likely to need the requested waivers in order to qualify for the discounted rates proposed, and the importance of the

volume of competitors' mail that is likely not to be eligible for equivalent or deeper discounts.

With respect to the effects of the waiver on competition generally, the Commission noted: "Nor does the record adequately address the question of whether the Postal Service's pricing proposal is likely to discourage market entry by an entrepreneur that might target that portion of the hybrid mail market that consists of mailings smaller than the volume thresholds for automation discounts." *Id.* at 27. Participants are requested to discuss this issue, and the issue of entry conditions for this market generally, as this information should help the Commission to determine the extent of latent, potential competition to Mailing Online.

Issue No. 2.

For the market test, the Commission approved the Postal Service's request for a waiver of the threshold volume requirements for automation basic discounts. The Commission indicated that there is a need for further inquiry during consideration of the experiment to determine whether the objectives of the waiver that the Postal Service requests for the experiment could be satisfactorily achieved in other ways. One possible alternative to the use of the eligibility waiver was suggested by the Commission in its market test Opinion. There the Commission noted that the record for the market test does not indicate whether it would be feasible to charge currently applicable mailstream rates to Mailing Online mailings that are initially under the current threshold volume requirements for automation discounts, and then make an appropriate rebate to the customer's account after batches are ultimately formed. PRC Op. MC98-1 (Phase 1) at 27. Participants are requested to comment on the feasibility and desirability of such an alternative, and to suggest any other alternatives to the use of this waiver that they consider feasible and desirable.

Issue No. 3.

For the market test, the Commission approved the Postal Service's request for a unilateral waiver of the threshold volume requirements for automation basic discounts. The Commission indicated that there is a need for further inquiry during consideration of the experiment to determine whether any waiver should be unilateral.

During consideration of the market test, Pitney Bowes proposed that the problem of allowing Mailing Online mailings special access to certain discounts be resolved by expanding the requested waivers to include any functionally equivalent "hybrid electronic postal service offered by a third party provider." See Pitney Bowes Brief at 1, 3, and Exhibit A. The Postal Service argued that Pitney Bowes' DirectNET hybrid service should not qualify for the expanded waiver that Pitney Bowes proposes, because it does not appear to be functionally equivalent to Mailing Online. The Service mentioned batching of jobs as a Mailing Online function that DirectNET does not perform. Postal Service Reply Brief at 6-7. Participants are asked to comment on whether, during the experiment, the waivers requested by the Postal Service should be extended to third-party providers of functionally equivalent hybrid mail services, or whether eligibility for such waivers should be determined by some other basis. In particular, parties are asked to comment on whether, in determining how eligibility for automation discounts should be expanded, it should be considered essential that mailings originate electronically, or whether lettershops or presort bureaus should qualify if they produce mailings that meet all the conditions of mailability that the mailings of Mailing Online or other hybrid services would be required to meet.

To better evaluate whether eligibility for waivers should be determined by functional equivalence, participants are requested to comment on what criteria should be used to determine functional equivalence. They are also requested to address the administrative feasibility of determining which third-party services meet the criteria selected for determining functional equivalence. For example, comments could discuss whether it would be feasible to establish a special permit system to certify third-party

services as functionally equivalent to Mailing Online and whether such a system would be sufficient to ensure that waivers would be appropriately limited to the competitors of Mailing Online.

Issue No. 4.

The Postal Service requested that the destination entry requirement for the DBMC discount be waived for Mailing Online Standard A mailings during the market test. The Commission did not accept this proposal for the market test, on the grounds that the market test was not configured to yield destination entry characteristics that would be representative of the experiment phase. PRC Op. MC98-1 (Phase 1) at 28. The Postal Service requests that this eligibility requirement be waived for Mailing Online mailings during the proposed experiment. The Postal Service recognizes that Mailing Online mailings will not be deposited at the destinating BMC at the beginning of the experiment phase. Request, Attachment A1 at 1, Tr. 2/343. It asserts, however, that by the end of the experiment, the Mailing Online network will be fully deployed, and argues that much of Mailing Online mail will be entered at its destinating BMC or SCF, making it appropriate to offer the DBMC discount during the experiment phase.

Tr. 2/343,672, USPS-T-5 at 12.

The Commission requests that participants discuss whether the objectives of the requested waiver could be accomplished in alternative ways that do not require making the DBMC discount available to Mailing Online mailings on different terms than the discount is available to its competitors.

Issue No. 5.

The Postal Service identifies no marketing costs that are specific to Mailing Online. Mailing Online, however, is expected to benefit from marketing programs planned for PostOffice Online, which will jointly promote Mailing Online, and other postal products. The Service argues that no portion of joint marketing costs should be attributed to Mailing Online. Tr. 4/881, Postal Service Brief at 24. Other parties have

requested that joint marketing costs be tracked and provided so that their relevance to Mailing Online costs and rates could be addressed during consideration of the experiment phase. MASA Brief at 5, OCA Brief at 29, Pitney Bowes Brief at 9-10. The Commission concurred. PRC Op. MC98-1 (Phase 1) at 48. Participants are requested to discuss whether joint marketing costs that promote Mailing Online should be attributed to Mailing Online, and how any such cost attribution should be quantified.

Issue No. 6.

The Postal Service proposes a 25 percent markup over contract printer costs and the \$0.001 per impression fee for network services. The Service argues that this markup should be compared to the markups on annual mailing fees and to the markups for other major special services. It also argues that because Mailing Online is a price sensitive experimental service in its start up phase, a "lower" rather than a "higher" markup is appropriate. Postal Service Brief at 10-11. The Commission concluded that a 25 percent markup is not unreasonable for the limited market test. The Commission, however, reached no conclusions concerning the appropriateness of a 25 percent markup for subsequent phases of Mailing Online. PRC Op. MC98-1 (Phase 1) at 33.

Participants are invited to develop the record further on the criteria that should be used to determine an appropriate markup for Mailing Online for the proposed experiment phase, including the relevance of historical markups for annual permit fees, other special services, and the system as a whole.

By the Commission.
(S E A L)



Margaret P. Crenshaw
Secretary