

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

COMPLAINT OF GAMEFLY, INC.)
)
) Docket No. C2009-1R

COMPETITIVE PRODUCT LIST)
ADDING ROUND-TRIP MAILER)
) Docket No. MC2013-57

COMPETITIVE PRODUCT LIST)
ADDING ROUND-TRIP MAILER)
(MC2013-57)) Docket No. CP2013-75

**MOTION OF GAMEFLY, INC., FOR RELIEF WITH RESPECT TO
THE AUGUST 22 “REPLY” COMMENTS OF THE POSTAL SERVICE
(August 26, 2013)**

GameFly, Inc. (“GameFly”) respectfully moves that the Commission (1) dismiss the Postal Service’s July 26, 2013, request to reclassify DVD mailers as a competitive product for failure to submit a *prima facie* case on July 26 or August 5; (2) strike the “reply” comments filed by the Postal Service on August 22; or (3) allow GameFly to respond to the August 22 “reply” comments 20 days after GameFly obtains access to the material that the Postal Service filed under seal in Library Reference USPS-MC2013-57/NP2 (or the successor library reference that the Postal Service states that it is filing today).

The mass of new material included in the Postal Service's August 22 comments—virtually all of which should have been included in the Postal Service's Request on July 26—represents a flagrant sandbag of GameFly and the other parties who oppose reclassification of DVD mailers as a competitive product. Instead of making the competitive showing required by 39 U.S.C. § 3642 and 39 C.F.R. § 3020.32 in the Postal Service's July 26 Request, as the rules required, the Postal Service withheld virtually all of its case until August 22, too late for other participants to respond. To protect GameFly's due process rights, the Commission should impose one or more of the following remedies:

(1) Dismiss the product transfer request. The Postal Service's failure to establish a prima facie case in its July 26 filing (or even in the supplemental filing that the Commission allowed the Postal Service to file on August 5) is a failure of proof that warrants dismissal of the case without requiring other parties to incur further costs responding to it, and requiring the Commission to waste further resources evaluating it.

(2) Strike the August 22 "reply" filing. The Postal Service's sandbagging tactics (made to advance a claim of effective competition that itself was extremely belated) are sufficiently egregious to warrant the extraordinary remedy of striking the August 22 material rather than the less drastic remedy of allowing other parties to respond.

(3) If the Commission is unwilling to grant the first two remedies, GameFly asks for 20 days to do so from the date when GameFly gains access to the supporting material that the Postal Service filed under seal (20 days is the interval allowed by the Commission between the July 26 Request and the August 15 deadline for comments by other participants).

(4) If the Commission chooses remedy (3), and the extended comment period leaves the Commission with too little time to rule on the product transfer request by September 30, the Commission should sever the request for a separate decision on a separate procedural track. In the interim, DVD mailers should retain their current classification within First-Class Mail, a market dominant product, and the price equalization should take effect on September 30, as scheduled. Due process requires at a minimum that GameFly receive a reasonable opportunity to respond to the sandbagged material. But due process also entitles GameFly, consistently with the decision in *GameFly, Inc. v. PRC*, 704 F.3d 145 (D.C. Cir. 2013), to relief from the Postal Service's unlawful discrimination without further delay. GameFly is entitled to both, and should not be required to sacrifice one for the other.

ARGUMENT

Before the Commission may approve a request to transfer a market dominant product to the competitive product list, the Postal Service must prove that it no longer "exercises sufficient market power that it can effectively set the price of such product substantially above costs, raise prices significantly, decrease quality, or decrease output, without risk of losing a significant level of business to other firms offerings similar products." 39 U.S.C. § 3642(b)(1) and 39 C.F.R. § 3020.32(d). In the context of DVD mail, this requires proof, *inter alia*, that DVD rental companies like GameFly, Netflix, CafeDVD and MMAVault have viable substitute means of distributing their content to consumers. That in turn depends on two subsidiary questions. The first is whether consumers regard the content available via alternative delivery channels such as electronic streaming or downloading, or rental kiosks such as Redbox, to be close

enough substitutes for the content available from the DVD rental libraries of GameFly and Netflix as to make an increase in the price of DVD mail self-defeating. The second is, if these alternative distribution channels were in fact good substitutes for DVDs-by-mail, whether an increase in the price of DVD mail would be passed on to consumers through higher rental prices for DVDs (as the Postal Service asserts), or whether the DVD rental companies would simply have to absorb the postage increases by accepting reduced margins. *Cf.*, GameFly Comments (Aug. 15, 2013) at 7-10 (citing authorities); USPS Reply Comments (Aug. 22, 2013) at 6-8 (same). The burden of proof on these issues rests with the Postal Service, the party that is seeking to change the status quo. 5 U.S.C. § 556(d); 39 C.F.R. § 3020.32(a); GameFly Comments at 10 (citing precedent); *Enterprise Products Partners L.P., and Enbridge Inc.*, 139 FERC ¶ 61,099 (2012) at Par. 33 (“The burden of proof is on the pipeline [that seeks exemption from maximum rate regulation on grounds of effective competition] to establish that it lacks significant market power in the relevant origin and destination markets through its petition, and when necessary, through the presentation of evidence at trial.”).

The Postal Service’s July 26 Request did not even attempt to meet this burden. The Postal Service’s initial “analysis” of the issue consisted of a single page of conclusory assertions, supported by a Bloomberg news story and few citations to Netflix’s most recent Form 10-K, supporting the unexceptionable observation that the audience for Internet video and rental kiosks has grown and the audience for DVDs-by-mail has shrunk. Monteith Statement (July 26, 2013) at 3-4. Nowhere in its July 26 filing did the Postal Service confront the central issue raised by the transfer proposal: whether the *remaining* millions of households that still choose to rent DVDs by mail from companies like Netflix and GameFly regard the content available from Internet

streaming and downloading, and Redbox rental kiosks, as acceptable substitutes for the enormous rental libraries of (1) video entertainment available by mail from Netflix or (2) high-powered, multi-gigabyte video games available by mail from GameFly. Likewise, the Postal Service provided no quantification whatsoever of the effect that increases in the postage charged for DVD mail would have on DVD mail volume or the Postal Service's revenues and net contribution from this mail. These are gaping holes in the Postal Service's case, particularly in light of the Postal Service's own data showing that First-Class Mail letters and flats, both single-piece and presorted, remain highly price-inelastic despite considerable loss of volume to the Internet. GameFly Comments (August 15, 2013) at 3-30. GameFly's observations on these points in its August 15 comments were foreseeable to anyone with even a basic knowledge of market dominance precedent.

The Postal Service's August 22 "reply" filing is as copious as the July 26 initial filing was thin. The discussion of competitive issues in the August 22 filing includes 21 pages of legal argument, a 13-page single-spaced declaration by Mark Shoeman, a purported expert on shipping and logistics, and a report—of unknown length, because the Postal Service filed it under seal—by IBISWorld, a commercial market analysis firm, on "the DVD, game, and video rental market in the United States." This mass of new material, unlike the Postal Service's July 26 filing, at least acknowledges the proof requirements of 39 U.S.C. § 3642(b)(1) and 39 C.F.R. § 3020.32(d). Material this elaborate in all likelihood was commissioned well before GameFly and Netflix filed their August 15 comments. In any event, regardless of when the material was prepared, it

should have been included in the Postal Service's initial Request, and not withheld until rebuttal.¹

The Postal Service's failure to make its case in its initial Request warrants dismissal of the Request for failure of proof. When the Postal Service fails to meet this burden in its initial filing, dismissal is the appropriate remedy. As the FERC held in a similar case,

Order No. 572 [the FERC's equivalent of 39 U.S.C. § 3642 and 39 C.F.R. § 3020.32] places the burden of proof on the applicant seeking market-based rate authority, and the Commission is not compelled to hold a hearing if such additional process is unwarranted.

Enterprise Products Partners L.P., supra, 139 FERC ¶ 61,099 at Par. 42 (citations omitted). Even after the August 22 "reply" filing, the Postal Service has still failed to quantify the impact of increases in DVD mail postage on DVD mail volume and the Postal Service's revenues and contribution from DVD mail.

Second, the sandbagged material should be stricken. The Commission has been generally reluctant to strike material of this kind, preferring the less drastic remedy of allowing injured parties to file surrebuttal. See, e.g., Presiding Officer's Ruling No.

¹ The cost analysis in the Postal Service's August 22 filing is also a sandbag. The Postal Service's July 26 Request included none of the cost and revenue data required by 39 U.S.C. § 3633 and 39 C.F.R. § 3015.3, prompting a Commission order directing the Postal Service to correct this omission in a supplemental filing. Order No. 1794 (July 30, 2013) at 3. Even so, the Postal Service's supplemental cost filing on August 5 contained numerous inputs and assumptions that were unsupported. See Sander Glick Decl. (August 15, 2013). As with the competitive analysis, the Postal Service withheld many key elements of its cost analysis, including responses to criticisms that should have been foreseen at the outset, until the August 22 filing (see reply declarations of Virginia J. Mayes and A. Thomas Bozzo).

C2009-1/17 (April 15, 2010) at 5 (first sentence). But the egregiousness of the Postal Service's conduct here—on an issue that the Postal Service belatedly injected into the case in the first place—warrants the more drastic remedy of striking the material.² The Postal Service's filing is not an isolated occurrence, but only the latest in a series of filings interposed for delay.

Third, if the Commission chooses to allow surrebuttal filings as the remedy, due process entitles GameFly to a reasonable period of time to prepare its response. *Mail Order Ass'n of America v. USPS*, 2 F.3d 408, 428-430 (D.C. Cir. 1993). As the Commission explained in Order No. 280 (issued May 18, 1979) at 27:

An adequate opportunity to rebut an opponent's case by evidence of one's own has always been considered a requirement of due process. *Ohio Bell Telephone Co. v. Public Utilities Comm. of Ohio*, 301 U.S. 292, 301-303 (1937); *Northeast Airlines, Inc. v. CAB*, 345 F.2d 484 (1st Cir. 1965), *cert. denied sub nom. Eastern Airlines, Inc. v. Northeast Airlines, Inc.*, 382 U.S. 845 (1965).

The true principle is that a party who has a sufficient interest or right at stake in a determination of governmental action should be entitled to an opportunity to know and to meet, with the weapons of rebuttal

² See 22 Wright & Graham, *Fed. Practice & Procedure* (2nd ed. 2012) at § 5164 & n. 135 (“if the court feels that the proffered evidence should have been offered as part of the party’s case-in-chief, rather than being held back to sandbag the opponent, the court can exclude the evidence as ‘improper rebuttal.’”); *id.* at § 5177.1 & nn. 9 & 10 (citing cases); 899 F.2d 47, 50 n. 4 (D.C. Cir. 1990) (“We require petitioners and appellants to raise all of their arguments in the opening brief to prevent ‘sandbagging’ of appellees and respondents and to provide opposing counsel the chance to respond.”); *Corbin v. Norfolk & Western Ry. Co.*, 856 F.2d 193 (6th Cir. 1988), 1988 WL 89341 (6th Cir. 1988) (unpublished opinion); *Southern California Edison and San Diego Gas and Electric Co.*, 50 FERC ¶ 63,012 (1990); *Union Pacific Corp. et al.—Control—Chicago & N.W. Transp. Co.*, 1994 WL 498541 (ICC 1994).

evidence, cross-examination, and argument, unfavorable evidence of adjudicative facts. . . .

Davis, Admin. Law Treatise, § 7.02 (1958),

Accordingly, GameFly asks that the due date for responses to the August 22 filing be set 20 days after GameFly and other participants are allowed to see the material filed by the Postal Service under seal in its nonpublic library references. This is essentially the same interval established by the Commission for responses to the Postal Service's July 26 Request. The importance of an adequate response period is underscored by the sweeping implications of the Postal Service's unprecedented transfer proposal: if the mere existence of electronic diversion were sufficient to justify reclassifying DVD mail as a competitive product, virtually every market dominant product not covered by the Private Express Statutes could be the subject of similar product transfer requests.

Finally, if the requested comment period leaves the Commission with too little time to render a considered decision by September 30, the date on which the Commission-prescribed rate equalization is to take effect, the product transfer request should be severed from Docket No. C2009-1R, the complaint docket, for separate consideration, and the September 30 rate adjustments prescribed by the Commission in Order Nos. 1763 and 1787 should take effect on September 30, while DVD mail is still classified as a market-dominant product within First-Class Mail.

GameFly recognizes that the Commission was hoping to rule on the product transfer issue before September 30, 2013, when the Postal Service must implement the rate equalization prescribed by the Commission. While this desire is understandable,

the resulting procedural schedule has given the Postal Service the ability to run out the clock by withholding key parts of the Postal Service's August 22 filing from opposing parties until too little time remains for them to prepare and file a response to the sandbagged material.

The Postal Service's mode of filing of the August 22 "reply" has had precisely this effect. The Postal Service filed much of its August 22 filing under seal as a nonpublic library reference, with no advance notice to GameFly that might have enabled it to obtain approval of GameFly's reviewing representatives from other participants beforehand (a procedure that should not have been controversial, since GameFly has used the same reviewing representatives, without objection by the Postal Service or Netflix, for several years). The August 22 Notice identified three entities with proprietary interests in the material filed by the Postal Service under seal: Netflix and GameFly (for their mail volume data), and IBISWorld, a commercial market analysis firm from whom the Postal Service bought a copyrighted report on "the DVD, game, and video rental market in the United States" on which the Postal Service's August 22 competitive analysis relies. GameFly duly obtained the consents of both the Postal Service and Netflix to allow GameFly's customary reviewing representatives to gain access to the material. Shortly before 4:30 pm on Friday, August 22, however, GameFly learned from the Commission's staff—not the Postal Service—that the Postal Service had belatedly claimed that the material filed under seal also included unspecified proprietary information about unnamed *other* customers of the Postal Service.

The Postal Service filed earlier today a notice withdrawing its August 22 notice of nonpublic filing, and refiled the material a few minutes ago, apparently minus the

information about the other customers, as library references USPS-LR-MC2013-57/NP3 through –NP6. Even under the best of circumstances, however, GameFly will not gain access to the proprietary material until late today or tomorrow—four or five days after the Postal Service filed its August 22 “reply” comments with the Commission.

Under the circumstances, the Postal Service’s desire for a ruling before September 30 on its product transfer request must give way to (1) GameFly’s right to a reasonable opportunity to respond to the material that the Postal Service included in its August 22 “reply” filing, *and* (2) GameFly’s right to relief, at long last, from the Postal Service’s unlawful discrimination as directed by the Court of Appeals in *GameFly, Inc. v. PRC*, 704 F.3d 145 (D.C. Cir. 2013). The Postal Service should not be allowed, by its delaying tactics, to force GameFly to choose one of these rights at the expense of the other.

CONCLUSION

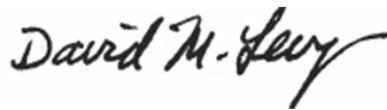
The Commission should impose one or more of the following remedies:

(1) Deny the Postal Service’s July 26 Request on the ground that the Postal Service’s July 26 and August 5 filings failed to establish a *prima facie* case under 39 U.S.C. § 3642 and 39 C.F.R. § 3020.32.

(2) Strike the Postal Service’s August 22 “reply” filing as an improper and abusive sandbag of material that should have been included in the Postal Service’s case-in-chief.

(3) Allow GameFly and other interested participants to file responses to the Postal Service's August 22 "reply" comments 20 days after the material filed under seal on August 22 is made available to GameFly's reviewing representatives. If the Commission determines that this relief leaves the Commission with too little time to evaluate the full record and rule on the Postal Service's July 26 product transfer request before the September 30 rate equalization remedy takes effect, the Commission should sever the product transfer request for a separate decision on a separate procedural track. In the interim, DVD mailers should retain their current classification within First-Class Mail, a market dominant product.

Respectfully submitted,

A handwritten signature in black ink that reads "David M. Levy". The signature is written in a cursive style with a long, sweeping tail on the letter "y".

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