

## CONCURRING OPINION OF COMMISSIONER GOLDWAY

I support the recommended decision, but with reservations.

I have long been a supporter of Postal Service innovation. For example, in remarks before the Direct Marketing Association's 1999 Government Affairs Conference (available on the PRC website) I favored permitting Postal Service experiments for new types of services that had a nexus to its core mission. I also have spoken out in favor of innovative pricing, such as seasonal discounts. I agree with the fundamental message of the opinion that selective discounts can be in the public interest. Furthermore, the legislative history behind the Postal Reorganization Act suggests that the PRC should work cooperatively with the Postal Service, and I do not want this agency to be a stumbling block to Postal Service innovation.

The Postal Service's first NSA proposal, though lawful, raises questions about the soundness of its business strategy. The Postal Service has ample authority to regulate the preparation and hygiene of its mail — the Domestic Mail Manual is filled with such examples. It is continually seeking solutions to address hygiene problems. Thus, the April 15, 2003 edition of DMNews online stated that the Postal Service in May will start reclaiming postage discounts from First-Class mailers who do not comply with its Move Update rules, citing as its source Angelo Wider, USPS manager of finance, in remarks at the New Orleans Spring National Postal Forum. Move Update is designed to reduce undeliverable as addressed mail, whereby mailers using automation or presort rates are required to update addresses every 180 days using USPS-approved methods. The same report cites other proposed changes that should improve address hygiene as well.

In this proceeding, Postal Service witness Plunkett states that the Service will be evaluating the type of hygiene program to which Capital One has agreed for possible wider implementation. But one wonders, once the Postal Service became aware of the alleged substantial benefits of such a program for one mailer why did it not ask itself — "Why not mandate specific hygiene practices for all First Class mailers using the medium

for advertising? Is it necessary or most efficient to give postage discounts to obtain what can be done by rule?" It is clear that Capital One likes to use First Class Mail for advertising and that barring some huge change in corporate strategy and fortunes such reliance will continue. It does not appear that Capital One was threatening to leave the First-Class mail advertising medium. See Tr. 4/714 (witness Plunkett), Tr. 2/70 (witness Jean).

The Postal Service has for some time wanted to be able to price its domestic product in the same way its private sector counterparts successfully do — by granting selective discounts to win or retain business. But there are major differences in how most private sector companies offer discounts to large accounts. First, private sector discounts are offered secretly so that other big customers do not demand the same or better deals, consequently eroding profit margins. Under the current system of postal regulation, where the Postal Service has been granted a monopoly, discounts cannot be made in secret. (Nor should a monopolist be able to price secretly.)

Second, discounts are offered based on specific competitive challenges ("I can't do business with you at that price — I've got a better offer.") and estimates of the customer's alternatives. Here, the evidence shows no specific competitive challenge, just the Postal Service's general desire to build volume. Indeed, with the current regulatory attacks on spam and telemarketing, some of the Postal Service's competitive threats to advertising mail could be lessened.

Third, private sector discounters know their costs of doing business with customers under the current arrangement and can assess any proposed new arrangement for its benefits to them, e.g., determining whether a discount will generate in fact scale economies. The evidence on this record concerns only hygiene related savings — there are no cost savings on this record associated with the potential for higher volumes . Even for those projected savings, Postal Service testimony shows it does not know with

much precision its current costs of handling Capital One's mail and how these costs will change under the future arrangement (e.g., the effect of PARS).

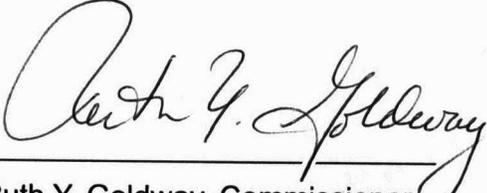
It may be that the Postal Service needs to reconsider its reliance on NSAs as the best option for pricing flexibility in the monopoly context and reconsider the niche classification approach, as some of the intervenors in this case suggest. The niche classification approach also reduces the possibility that discrimination will occur against mailers whose volumes are smaller and who cannot afford the litigation transaction costs of supporting an individual NSA, or the discrimination that could occur if the Postal Service focuses its (admittedly) limited negotiation resources on just the largest mailers. I would note that the Postal Service has pricing freedom for its international mail business, yet this practice does not appear to have helped it measurably, as volumes, revenues, and profits are declining in this sector.

This case profited from the observations of economists Panzar and Eakin concerning potential economic effects of the discounts available under the NSA on competitors of Capital One. Commission deliberations would be facilitated in future cases if the Postal Service analysts examined more thoroughly the current competitive conditions in the industry in which the NSA was being sought. For example, industry concentration, entry and exit conditions and other factors may indicate, e.g., that the slight advantage granted to one player in an industry from a lower rate will have merely the effect of a pebble thrown into a large lake — a mere ripple that soon disappears. Analysis of the credit card industry might show that there are a large group of well financed competitors, many of whom have their own particular competitive advantages (e.g., retailers who can advertise credit cards in their stores).

In light of the overall modest amount of money involved in this case (in relation to the Postal Service's total budget) and the economic experts' views about the potential benefits of contractual rates I am persuaded that new arrangements of this nature should

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be encouraged. However, I do not regard this case as precedent except for the general proposition that NSAs can be beneficial, and would ask the Postal Service and Board of Governors to carefully consider my reservations.



Ruth Y. Goldway, Commissioner