Postal Regulatory Commission

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Press Release

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Washington, DC –

Postal Regulatory Commission Sends Bank of America NSA to Postal Governors

The Postal Regulatory Commission today issued its Opinion enabling the Governors of the U.S. Postal Service to provide a final review of the proposed Negotiated Service Agreement between the Postal Service and the Bank of America Corporation (Docket No. MC2007-1).

"While the Commission found the agreement in compliance with the requirements of the Postal Accountability and Enhance Act (PAEA), we also found that the agreement could cost the Postal Service anywhere from $25 million to $45.8 million should the Governors move forward with the agreement," said Commission Chairman Dan G. Blair.

"We hope the Governors will carefully review the findings in the Commission Opinion in making its final decision on whether to adopt the agreement," said Blair.

Under the proposed agreement, Bank of America would use improved address barcode technology in exchange for discounted postage rates. A principal feature of the proposal would be the commitment by Bank of America to use the Intelligent Mail Barcode (IMB) system, and other new systems, designed to facilitate mail acceptance and processing.

The Postal Service expects IMB to play a critical role in the measurement of the service standards it is developing in consultation with the Commission. Because the PAEA requires the Commission to report annually on how well the Postal Service is meeting its service standards goals, testing IMB and other advanced programs now will benefit all postal customers. Both these benefits and the potential financial losses from this proposed agreement will be weighed by the Governors.

The Commission found that claimed savings of $5.5 million produced by this agreement were based on 1999 read/accept rates. The Commission proceedings uncovered more recent read/accept rates from 2006 and 2007. When the more recent information is used, it shows that the Postal Service stands to lose $25 to $45.8 million should the agreement be implemented.

"Congress, through the PAEA, granted the Postal Service greater autonomy to set its own rates and enter into NSAs. The Act requires that such agreements either improve the net financial position of the Postal Service or enhance its operations. The Postal Governors will have to make the final decision of whether this agreement makes good business sense for the Postal Service," concluded Blair.

The Commission noted in its Opinion "...that read/accept rates have improved to such an extent that Bank of America will not have to make any improvements in barcode readability to receive all available mail processing performance discounts." The Commission also cautioned that because the Postal Service will require "...the use of IMB for all automation discount mail in the near future, incentives under this Agreement would be paid to Bank of America while other mailers may be being required to adopt the same mailing practices without similar incentives."

The Commission's Opinion was issued on a 4-1 vote, with Vice Chairman Dawn Tisdale dissenting. Attached is the summary of the Opinion, concurring opinion by Commissioner Ruth Goldway, and Vice Chairman Tisdale's dissent. The Opinion is available on the Commission's website at www.prc.gov.

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The Postal Regulatory Commission is an independent federal agency comprised of five Presidentially-appointed and Senate-confirmed Commissioners, each serving terms of six years. The Chairman is designated by the President. In addition to Chairman Blair, the other four Commissioners are Ruth Goldway, Tony Hammond, Dawn Tisdale, and Mark Acton.

I. INTRODUCTION AND SUMMARY

[1001] The Postal Service and the Commission are in the process of transitioning to operation under the Postal Accountability and Enhancement Act of 2006 (PAEA). Congress directed the Commission to provide a system of modern rate regulation that recognizes the desirability of special classifications that improve either the net financial position or operations of the Postal Service. The Postal Service has been given broad rate and classification authority to act within that system.

[1002] These overarching reform priorities are the reason the Commission provides a recommendation of the Postal Service's request for a Negotiated Service Agreement with Bank of America. 39 U.S.C. §§ 3622(b)(9) and 3623(c)(6). At the same time, the Commission strongly cautions the Governors that several significant financial concerns related to this Agreement have come to light. This independent evaluation should be used by the Governors to inform their decision on whether or not to proceed with this Agreement.

[1003] This Negotiated Service Agreement is described in the Postal Service request as a pay-for-performance agreement that will produce a $5.5 million net benefit. As described, Bank of America commits to implement several advanced mailing practices, and is provided discounts for proven performance improvements relative to six negotiated baselines. Two of these baselines, those for First-Class Mail and Standard Mail read/accept rates, govern the vast majority of potential cost savings to the Postal Service and discounts paid to Bank of America.

[1004] In its request, the Postal Service explains it has no information on Bank of America's actual read/accept rates. It chooses to use 1999 data for read/accept rates to develop these baselines.

[1005] Read/accept rates have improved steadily since 1999. Through the diligent discovery efforts of an employee organization, recent, reliable Postal Service read/accept rate data from 2006 and 2007 surfaced. The Commission concludes that read/accept rates have improved to such an extent that Bank of America will not have to make any improvements in barcode readability to receive all available mail processing performance discounts. This is not indicative of a pay-for-performance agreement.

[1006] Applying the most recent read/accept rates, assuming that Bank of America continues to perform at systemwide average levels, and generally accepting the Postal Service's estimates relating to the other four incentive discounts, the financial analysis reveals that the Postal Service will lose up to $45.8 million from the Agreement. Even in the unlikely event that Bank of America achieves perfect read/accept rates, the Postal Service will lose more than $25 million from the Agreement.

[1007] Faced with such arguments, the Postal Service on brief contends that the Commission should look at the other benefits that it may obtain through this Agreement. The evidentiary record provides no substantive qualitative or quantitative insight into how to measure such benefits. The Governors must balance these unspecified operations benefits against the financial losses identified by the Commission in this opinion.

[1008] Additional problems with this Agreement must be considered. Other mailers are in ongoing pilot tests of various features of this Agreement for which they receive no incentives. Also, the Postal Service has announced its intention to mandate use of Intelligent Mail Barcodes for all automation discount mail in the near future. Incentives under this Agreement would be paid to Bank of America while other mailers may be required to adopt the same mailing practices without similar incentives. As a result, many mailers similarly situated to Bank of America may qualify for functionally equivalent agreements, and demand equivalent discounts even after these mailing practices become mandatory. The Postal Service has expressed its intent to make comparable agreements available to similarly situated mailers. This reduces the possibility that other mailers would find the Agreement discriminatory, but increases the financial risk to the Postal Service as it may have to provide substantial additional rate incentives for mandated practices.

[1009] This situation raises many concerns over the practices and procedures that are in place for developing successful negotiated agreements. The Commission reaches its findings by examining information that is readily available at the Postal

Service. Yet the personnel negotiating and the officers reviewing this Agreement apparently were unaware of the existence of this data before filing the request and even following several months of litigation.

[1010]   The PAEA clearly contemplates that Postal Service management will be responsible for developing pricing strategies. In this new environment, price caps will limit the Postal Service's ability to recapture the losses associated with bad business decisions.

[1011]   With the more limited Commission pre-implementation review under the PAEA, the burden of thoroughly reviewing new agreements has shifted to the Postal Service. To facilitate this shift in responsibilities, the Postal Service must ensure effective communication between those developing and approving Negotiated Service Agreements and the operational organizations that have the technical knowledge to assure successful agreements.

[1012]   Moreover, it is imperative that the Postal Service develop and adopt review procedures, at the highest levels, to assure that the agreements make business and economic sense. Multi-million dollar Negotiated Service Agreements should receive careful internal scrutiny comparable to decisions to purchase major facilities or expensive equipment systems.

CONCURRING OPINION OF COMMISSIONER GOLDWAY

The new PAEA provides the Postal Service with the flexibility to adjust rates within classes of mail for market-dominant products, adopt special classifications that improve the net financial position or increase the efficiency of operations, and to price and market competitive products to accrue profits.

It also gives the PRC expanded oversight with regard to the financial soundness, efficiency, and fairness of Postal Service operations.

The negotiated service agreement (NSA) before the Commission demonstrates that the Postal Service is not yet capable of negotiating a good bargain within the framework of the PAEA. The Commission's majority opinion points out serious shortcomings in Postal Service management decision making. First, and foremost, through this NSA, the Postal Service will lose between $25 and $45 million and opens itself — if it is to be fair to other similarly situated mailers — to lose much more.

Second, the record of the case indicates that Postal Service negotiators did not prepare themselves with all the necessary financial and costing data when conducting the bargaining process with Bank of America. And third, the complex bureaucracy of the Postal Service has not yet been capable of identifying, analyzing, and distributing the appropriate data needed to make accurate cost-benefit decisions, nor did it pass on the data it did have to the group assigned to enter into negotiations for the NSA.[1]

[1] Robinson, et al., *Negotiated Volume Discounts in a Regulated Post*, available on the Commission's website, *www.prc.gov*, provides an instructive analysis of the impact of previously approved negotiated service agreements.

This is the first opportunity the Commission has had to act on an NSA since passage of the new law.[2] I appreciate that my fellow Commissioners want to show their support for the concepts embodied in the new law and express their willingness to give the flexibility to the Postal Service provided therein. In the scheme of a $75 billion budget, it will not be significant if the Postal Service loses $45 million on an experimental venture. Therefore, I am willing to go along with the majority and approve the Bank of America NSA.

However, I feel obliged to emphasize that the flaws identified above in the Postal Service/business bargaining process do not bode well for the Postal Service under the PAEA regime. Unless the Postal Service takes the cautionary advice provided within the Commission's opinion, it may find it difficult to participate in a significant number of NSAs and still operate within the price cap, much less be optimistic that profits can be made in the competitive products sector.

I commend Commissioner Tisdale, the only one of my fellow Commissioners with direct operational experience at the Postal Service, for his forthright dissent. I am hopeful that his strong statement and my more detailed description of the concerns he identified will prove helpful to the Postal Service.

Ruth Y. Goldway, Commissioner

[2] I recognize that the PAEA system of rate regulation has not yet been implemented, so that this request arguably could have been evaluated giving less weight to the new legislation.

DISSENTING OPINION OF VICE-CHAIRMAN TISDALE

I and my colleagues have long been strong supporters of negotiated service agreements. It is sound policy to encourage agreements designed to take advantage of special situations that should benefit the Postal Service and one or more private sector partners, without harming either competitors or other mail users.

My review of the evidence in this case leads me to conclude that the proposed arrangement with Bank of America is not such an agreement. I do not reach this conclusion simply because the Postal Service “might” lose money. I realize that businesses enter into many contracts with knowledge that future events may lead to unexpected results.

In this instance, the Postal Service has information showing that this is a bad deal financially that is likely to be viewed by other mailers as discriminatory. It is too certain that the Postal Service will lose money, and certain that the losses will be too substantial, between $25 - $45 million, for me to recommend this agreement.

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Dawn A. Tisdale, Vice Chairman