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POSTAGE RATES FOR PRIORITY MAIL

By DAVID S. STANLEY†

I. INTRODUCTION

THE CONCEPT of integration which is interwoven with our social structure has become part of the thinking of the Post Office Department. According to present plans, the Postmaster General will ask Congress for authority to merge domestic first-class and airmail into a single category to be known as "priority" mail. This would be dispatched by the most expeditious means of transportation and would presumably include letters, sealed packages, government postal, and private post cards.

Air transportation of letters and cards bearing only first-class domestic postage began 6 October 1953, with service between New York, Newark-Chicago, and Washington-Chicago. This mail was carried on a "space available" basis, and received none of the priorities given letters and cards sent at airmail postage rates. The service has been expanded throughout the continental United States as well as Alaska, Hawaii, and other off-shore points such as Mexico and Canada. According to the Postmaster General's report for 1967, this non-priority mail service has advanced letter delivery from one to three days among the principal cities of the southern tier of states.

Indicative of the growth of this operation is its increased proportion of total domestic airline mail ton-miles. In 1954, the first complete year of operation, non-priority (first-class) mail ton-miles were 14 percent of the total; in 1967, this proportion had grown to 31 percent, based upon the CAB's *Air Carrier Traffic Statistics*, December 1955 and 1967. Now nearly all such mail going over 200 miles is carried by air.

The Post Office Department's proposal is based in part at least, upon the continued attrition of railroad passenger service, whose trains include Railway Post Office cars. Train schedules have become unsuited to Post Office Department requirements and, according to the Department, this development has caused a diversion of mail from trains to other types of carriers. Whether discontinuance of train service has been caused by the Department's removal of Railway Post Office cars, or whether the latter were taken off because of the railroads' dropping of trains, is a question beyond the purview of the present article.

Adoption of the priority mail program will probably involve the setting of a new postage rate for the service. A letter charge of seven or eight cents an ounce or fraction has been suggested, according to the *Wall Street*

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Journal of 22 April 1968, but no details as to how this rate was arrived at were available. What the postage will be for cards has not been stated.

Since the priority service is designed to expedite carriage of first-class and airmail by the medium or combination which offers the fastest transport, it would presumably exclude local operations. A letter or card sent from city to suburb might have a choice between truck or helicopter service, or possibly bus, but an intra-city delivery would be unaffected by the establishment of a priority category. It would therefore appear in order to retain the present postage rates per ounce or fraction of 6 cents and 5 cents, respectively, for letters and cards sent to a local destination. Whether there should be the separate priority and non-priority classes as indicated, is a policy question for Congress to decide.

II. BASES FOR SETTING POSTAGE RATES

Before computing a priority rate which can be justified on other than arbitrary grounds, it is desirable to examine the economic standards which may be used to set postal charges. Those standards are listed and discussed in the report of the President's Commission on Postal Organization, which considers the Post Office as being essentially a public utility.¹ These standards are:

(1) Budget standard which is the requirement that postal revenue as a whole should equal costs as a whole, with the exception of "public service" costs. This directive is set forth in the Declaration of Policy embodied in the Postal Service Act of 1958,² with "public service costs" excluded.³ It may be noted that the budgetary standard sets a floor as well as a ceiling on postage rates.

(2) Cost of service which involves problems of allocating equitably and economically justifiably, postal costs to the various classes of mail. Each class should bear the actual cost of providing its specific service, as well as its share of "institutional" costs. The latter are those costs which vary little with the volume of a particular class of mail, but are the costs of maintaining the postal system per se. Such costs are related to other factors such as growth of population and its density.⁴

Currently, the Post Office Department uses a cost ascertainment system almost a half century old to determine revenue, volume and cost of each class of mail. Costs are determined on the basis of full distribution, by which every postal expense is assigned to some class of mail or special service. This methodology ignores the "intangible" costs such as priority of service accorded first-class and airmail, preferred treatment in post offices and in transit, value of service to user, and privacy accorded these

¹ THE REPORT OF THE PRESIDENT'S COMMISSION ON POSTAL ORGANIZATION, TOWARDS POSTAL EXCELLENCE [hereinafter cited as POSTAL EXCELLENCE] 122-32 (June 1968).

² The Postal Service (1958), as amended, 39 U.S.C. § 2302 (1964).

³ Public service and related costs include the loss resulting from free or reduced rate transmission of mail matter, reduced rates for certain publications, part of costs of operating third and fourth-class post offices, star and rural routes, performance of non-postal and special services, additional cost of carrying U.S. mail by foreign carriers at Universal Postal Union rates above that prescribed for U.S. airlines. The Postal Service, (1958), as amended, 39 U.S.C. § 2303 (1964).

⁴ POSTAL EXCELLENCE, *supra* note 1, at 131.

mail categories. The Declaration of Policy directs that these factors be taken into account in setting first-class and airmail postage rates, but specifies no formula for their evaluation.⁵

Some years ago a department witness, Deputy Postmaster General Stans, testifying before a sub-committee of the Senate Post Office and Civil Service Committee, submitted a table indicating that allocated mail costs should be increased by 32 percent to allow for the preferred treatment accorded first-class and airmail. The handling of first-class mail entails extra expenditures, not required if such mail were not accorded such treatment. Otherwise, it would be unnecessary to pay for night or Christmas overtime, nor would extra collections or delivery be made during the pre-Holiday period. First-class mail is responsible also for overtime put in by night employees who may "work" second and third-class mail to some extent. Thus, some of the extra expense caused by first-class mail processing may be reflected in charges to the other classes.⁶

(3) Value of service is the least susceptible to quantitative measurement of any of the three standards mentioned in the report of the Commission on Postal Organization. It is used in the sense that it measures what a service is worth to the user.

The requirement that long-run variable costs be covered establishes a price floor for a particular class of mail, but the upper limit or ceiling would be set by the demand for the service. The phrase "would be set" is used advisedly, since in the case of first-class and airmail no one knows for sure what the ceiling postage rate might be. For second, third and fourth-class or parcel post, shippers could have a choice of using express or private trucking if the postal rates were set at a level which would make switching to commercial carriers economically desirable.⁷

But for first-class and airmail, the Post Office Department has a monopoly. Congress could prescribe a postage rate far beyond a concept of reasonableness by any criterion, and postal service users would just have to "grin and bear it." Theoretically, the telephone and telegraph compete with the mail, but they do not offer a practical alternative due to the great rate differentials. This is illustrated by the following tabulation of telephone and telegraph rates, Washington to Los Angeles, submitted by a witness during the House hearings on the Postal Revenue Act of 1967:⁸

	<i>Day</i>	<i>Evening</i>	<i>Night</i>
Telephone, station-station (3 min.)	\$2.00 plus tax	6-8 PM \$1.50	\$1.00
Western Union (50 words)	3.14		1.90

These compare with a domestic postage rate per ounce or fraction of six

⁵ The Postal Service (1958), as amended, 39 U.S.C. § 2302 (1964).

⁶ See the testimony of Maurice H. Stans, Deputy Postmaster General, *Hearings on H.R. 5836, 7910 and S. 1916 Before the Subcomm. on the House Comm. on Post Office and Civil Service*, 85th Cong., 1st & 2nd Sess. 29-31 (1957).

⁷ There is a private service in Oklahoma City which delivers unaddressed fliers, grocery circulars and the like, by prior arrangements with several clients.

⁸ See the testimony of Harry J. Maginnis, President, Associated Third-Class Mail Users, *Hearings on H.R. 7977 and 7978 Before the Subcomm. of the House Comm. on Post Office and Civil Service*, 90th Cong. 1st Sess. 635 (1967).

cents first-class, ten cents airmail; the rates for first-class and airmail cards are five cents and eight cents, respectively.

The foregoing discussion is centered on the value of service principle in its relation to mail rates, compared with those of other communication or transportation media. Within the postal system itself, strength of demand varies for the several mail classifications,⁹ as do differences in handling and service. These differences will be reflected in the long-run variable costs assigned to each class. Unfortunately value of service data are scanty, if not lacking entirely, but it is significant that under the Post Office Department cost ascertainment procedure, only first-class and airmail cover their fully allocated costs. These are the classes which enjoy the highest priorities and preferential treatment accorded the various mail categories of the Postal System and which for fiscal 1967 accounted for 56 percent of all mail in terms of number of pieces and postal revenue.¹⁰

What the user will pay for postal service has never been determined, as mentioned earlier. Based on past experience with rate increases, demand for first and third-class mail seems relatively inelastic, and postage raises have produced additional revenue. However, the absolute amount of past raises has been small, and the effect of various unknown factors on mail volume has rendered invalid any conclusions as to the elasticity of demand.¹¹

III. SELECTION OF A RATE STANDARD

For the purposes of this article, it appears that cost coverage by revenue is the best choice as a criterion for a postage rate. The budget standard is not specific for individual classes and value of service from a practical standpoint, is probably indeterminate. Were this not so a value of service postage rate might be the prime selection from an economic point of view.

At present the only postal cost data available are those furnished by the Post Office Cost Ascertainment System. Functional cost assignment as opposed to fully allocated expense is not a part of the System and no account is taken of the existence of a large segment of institutional costs. These are not assignable to any particular mail category but belong to the postal system as a whole, as mentioned earlier. This deficiency reinforces the desirability and indeed need for a more sophisticated cost accounting system than is now employed by the Post Office Department.

IV. HOW THE PRIORITY RATE IS DETERMINED

The methodology employed in the present study is to determine the combined first-class-airmail volume, revenue and allocated cost, using experience over the 1963-67 period as a base, at the postage rates then pre-

⁹ It may be mentioned that value of service does enter in a comparison of first-class and air mail postage rates. The differences between the two rates is a measure of how much the mail user values the *guaranteed* speedier transportation of the air mail letter or card, relative to that of ordinary first-class mail. As mentioned earlier, a goodly proportion of the latter class does go by air on a space available basis.

¹⁰ POSTAL EXCELLENCE, *supra* note 1, at 125.

¹¹ *Id.* at 134.

vailing. From this the revenue at the present postage rates and cost for fiscal 1968 are estimated, giving the corresponding cost coverage. Finally, the letter rate necessary to give this coverage is computed. A rate for priority postal and post cards has been included also.

In adopting this procedure it is assumed that the revenue and cost for priority mail can be calculated as a combination of first-class and air, with no significant difference in the Post Office cost ascertainment allocation methodology. The priority rate determination is based upon such information as is available and more complete data incorporated in a modern sophisticated cost accounting system might produce a postage rate different from that herein derived.

V. METHODOLOGY AND DISCUSSION OF RESULTS

Table 1 gives the basic data from which the priority postage rate was computed for non-local letters and cards. Volume, revenue, and cost data are for domestic mail during the five-year period, 1963-67, with projections for the second half of fiscal 1968. Constructive revenue is that which would be generated, if each pound of first-class and airmail contained only pieces weighing whole ounces. It is derived by multiplying the postage rate per ounce or fraction for a given year by 16 (the number of ounces in a pound) and then by the pound volume for that year. When a postage rate changes in the middle of the fiscal year as took place in 1963 and 1968, the postage rate applying to each half of the year was multiplied by the number of pounds transported during each of those periods, and an annual total then compiled. For 1968, projections have been made for the last half of the year. Since cards are charged at a piece rate, rather than by weight, constructive and actual revenues are the same. Piece volume for letters and sealed packages is included in the table in case it is desired to use this basis, instead of weight, for computing a priority postage rate.

In making projections for fiscal 1968, piece and weight volume, as well as cost for letters have been computed by determining the average annual gain during the 1963-67 period. Projections are then made only for the second half of fiscal 1968 by using the ratio of the same period for 1963 to the total of that year. The reason for this step is that the latest postage rate change was not effective until 1 January 1968. Since a former change took place in the middle of fiscal 1963, the ratio mentioned was applied to the projected 1968 data. It is believed that this procedure takes into account any variations in volume which might result from an increased postage rate. The projected six-month cost is taken as 50 percent of the 1968 total on the assumption that a postage change has little, if any, effect on this factor. Constructive revenue for the projected six-month period is then calculated as indicated in the paragraph above.

For postal and post cards, projections of volume revenue and cost are more difficult to make on a justifiable basis. It will be noted from Table 1 that with the exception of airmail number of pieces, the trends over the five-year period have been irregular, thus rendering inapplicable the

TABLE 1
NON-LOCAL VOLUME, REVENUE AND COST—DOMESTIC FIRST-CLASS AND AIR MAIL, 1963-67 FISCAL YEARS AND
1968 PROJECTED (JAN. 1-JUNE 30)
LETTERS AND SEALED PACKAGES

	Number of Pieces (millions)		Number of Pounds (millions)		Constructive Revenue ¹ (millions)		Actual Revenue (millions)		Allocated Cost (millions)	
	First Class	Air Mail	First Class	Air Mail	First Class	Air Mail	First Class	Air Mail	First Class	Air Mail
	1963	21105.2	1487.1	751.2	60.4	\$ 538	\$ 72	\$1144.4	\$141.2	\$1064.0
1964	21850.4	1442.1	789.2	61.4	505	79	1327.6	148.6	1145.0	141.7
1965	22911.3	1560.4	848.0	68.5	542	88	1402.3	165.5	1257.6	153.0
1966	24609.0	1752.1	916.5	76.7	584	98	1507.5	184.2	1403.8	170.2
1967	26021.7	2014.1	1005.7	87.6	640	112	1595.6	207.5	1575.9	202.2
Total	116497.6	8255.8	4310.6	354.6	\$2909	\$449	\$6977.4	\$847.0	\$6446.3	\$804.9
1968 (Jan.-July) Projected ²	12700	960	510	40	\$ 490	\$ 60	—	—	\$ 840	\$ 110
	1481.9	24.9	Postal and Post Cards ³				\$	\$ 51.5	\$ 1.4	\$ 66.1
1964	1552.2	26.3	Not relevant		Same as actual			62.2	1.6	71.8
1965	1400.4	27.6						56.2	1.7	67.7
1966	1340.7	28.5						53.7	1.7	68.0
1967	1500.9	37.8						61.4	2.4	81.1
1968 (Jan.-July) Projected	710	17						\$ 35 ⁴	\$ 1 ⁴	\$ 37
(1966-67 semi-annual ave.)										

¹ Revenue generated if each pound of mail contained only pieces weighing whole ounces. Computed by multiplying postage rate per oz. or fraction x 16, by number of pounds. Letter and sealed package rates, fiscal 1963-68 were as follows: July 1, 1962-Jan. 7, 1963, 4 cents first-class, 7 cents air mail; Jan. 7, 1963-Jan. 1, 1968 5 cents first-class, 8 cents air mail; Jan. 1, 1968 6 cents first-class, 10 cents air mail. Computation indicated takes into account postage rate changes during fiscal years. The corresponding rates for cards were: 7/1/62-1/7/63, 3 and 5; 1/7/63-1/1/68, 4 and 6; 1/1/68-5 and 8 cents per piece.

² Volume and cost for entire 1968 computed on basis of average annual gain 1963-67. Volume for last part of 1968, Jan. 1-June 30, then calculated on basis of relation of 2nd half of 1963 to year's total. As noted above, a rate change occurred Jan. 7, 1963, and another on Jan. 1, 1968. Cost for last 6 mos. of 1968, 50 percent of annual total.

³ Postal cards are Government printed and sold; post cards are printed and sold by private business.

⁴ Number of pieces x current postage rate.

Source: U.S. Post Office Department — Cost Ascertainment Report, 1963-67.

method used for letters and sealed packages. In view of this circumstance it was decided to make projections by taking a semi-annual average for 1966 and 1967, the last two years of the period. No projections were made for weight volume since this factor has no relevance to card revenue. As mentioned earlier, constructive and actual revenues are identical for cards and have been computed by multiplying the projected number of pieces for first-class and air mail by the current piece rates of 5 cents and 8 cents, respectively.

Since cost for airmail cards is not segregated from that of letters, only the cost for first-class cards is available. It is thus impractical to determine whether any cost trend existed during 1963-1967 for airmail cards, separate from that of letters and sealed packages.

Table 2 gives the data of Table 1, as totals of first-class and airmail to create the priority mail category. In addition, two other series are shown, namely the relationship of actual to constructive revenue for letters and sealed packages, and the cost coverage for both letters and cards.

The actual-constructive revenue ratio is significant for two reasons. First, it measures the substantial margin resulting from the charging of ounce fractions at the same rate as whole ounces. Second, and more important, the ratio is the basis for determining the priority postage rate, as will be shown in a later paragraph.

Cost coverage by revenue is, of course, important, especially since it has been selected for present purposes as the criterion for constructing a priority postage rate. It will be noted that for letters actual revenue has exceeded cost from 2 to 14 percent over the 1963-67 period, with an average of 8 percent. For the projected last six months of 1968, the cost coverage is indicated as 139 percent, a ratio which is probably above that which would be derived if actual data were available. In the case of cards, the table shows that this type of mail has been handled consistently at a loss. However, the projected data suggest that a nearly break-even operation for priority mail would result if the current postage rates for first-class and airmail cards are applied to the respective projected piece volumes, and the results combined for the priority category.

As mentioned earlier, it has been assumed that revenue and costs for first-class and airmail can be combined for priority mail with no significant changes in the Post Office Department's method of allocation. Subject to this limitation, the final step is to calculate the priority postage rate.

VI. THE PRIORITY POSTAGE RATE

Taking letters and sealed packages first, Table 2 shows that the projected constructive revenue for January-July of 1968 is \$550 million. During this period there was an estimated weight volume of 550 million pounds, giving a yield of \$1 per pound. This is equivalent to an ounce yield of 6.25 cents, and applying the actual-constructive revenue ratio for 1963-67 of 240 percent, this rate would result in a total actual revenue of \$1,320 million. The estimated allocated cost of \$950 million would thus

be covered by a margin of 39 percent, as shown in the last column of the table.

Since rates are expressed in whole numbers, the proposed priority postage for each ounce or fraction would be either 6 cents or 7 cents. If the former, the margin would be reduced to 33 percent, as compared with a margin of 56 percent for a 7 cent postage rate.

Turning to postal and postcards, the estimated revenue per piece was 4.95 cents, or practically identical with the current 5 cent postage rate for first-class cards. If the priority rate be increased to an even 5 cents, revenue would cover cost to the extent of 98 percent, compared with the coverage of 97 percent shown in Table 2. If the rate were raised to 6 cents cost coverage would be 118 percent.

As may be noted for both letters and cards, the computed postage rates for priority mail are very close to those currently in effect for first-class mail alone. Such a result is to be expected in view of the large proportion of weight and piece volume represented by this class. It should be mentioned, however, that a large amount of non-local mail bearing only first-class postage does actually go by air, although the actual figures are not available. The Cost Ascertainment Report of the Post Office Department makes no separation between surface first-class and "non-priority" first-class mail which is airborne when plane space so allows.

VII. SUMMARY AND CONCLUSIONS

The Post Office Department has proposed to merge first-class and airmail into a single category to be known as "priority mail." This would be sent to its destination by the most expeditious transportation possible. For some time mail bearing only first-class postage has been carried by air to several parts of the country, when space was available on planes.

Adoption of the proposal mentioned will probably require the setting of a new mail rate. Since the program would presumably affect only non-local mail, it would seem logical to apply the new rate solely to that type of operation. Such a rate could be set on one of several bases including budget standard, cost of service, and value of service. The first of these requires that postal revenue as a whole equals costs as a whole, excluding "public service" costs. Such a base is not specific for individual classes of mail and is unsatisfactory for present purposes. Value of service, or what the service is worth to the user, could be the most satisfactory basis were it determined or determinate. Cost of service is thus the remaining choice and has been adopted for the purposes of this study.

The procedure for determining the rate in question combines first-class and airmail volume revenue and Post Office Department allocated costs, using the 1963-67 period experience as a base. From this, projections were made for the second 6 months of fiscal 1968 since no actual data were available. It is assumed that first-class and airmail data can be combined for the priority category, with no significant changes in the Department's

allocation methods. The period mentioned was chosen because the present postage rates became effective January 1 of fiscal 1968.

Postal revenue may be considered as made up of two parts: First, that which would be derived if each pound of mail consisted only of pieces weighing whole ounces, termed "constructive revenue"; and second, the excess over that figure due to the practice of charging fractions at whole ounce rates. This division applies only to letters and sealed packages since postal and postcards are charged by the piece.

Since first-class and airmail (including air parcel post) are the only classes of postal matter with an excess of revenue over cost, the substantial revenue margin given above for a 7 cent priority rate would be helpful in reducing the deficits incurred by second, third and fourth-class mail. As for cards, a 6 cent rate would provide the same benefits. Actually card revenue is but a small part of that from letters (Table 1), and whether the rate is 5 or 6 cents is relatively unimportant.

It should be kept in mind that a large proportion of mail bearing only first-class postage already goes by air, even though it is not so designated in the Cost Ascertainment Report. Hence, a priority mail class would, to a great extent, merely recognize this fact officially, but with the added feature that all such mail would be guaranteed the fastest dispatch possible.