

By Robert W. Mitchell

Editors Note: This article is based in part on a paper entitled "Postal Worksharing: Welfare, Technical Efficiency, and Pareto Optimality," presented at the Sixth Conference on Postal and Delivery Economics, Montreux, Switzerland in June 1998. The opinions expressed are those of the author and do not necessarily represent opinions or positions of the Postal Rate Commission.

Since the Postal Reorganization Act of 1970, postal rates in the United States have been set following hearings before the Postal Rate Commission. Based on detailed testimony from the Postal Service and others, including extensive input from mailers and mailing organizations, the changes that have occurred in the rate structure have been enormous. Whereas rates for all classes were once relatively simple, they are now extremely complex. Specifically, we now have presort rates, barcode rates, automation rates, drop ship rates, letter/flat rate differentials and saturation rates, among others. Mailers are dependent on complex computer systems to not only prepare their mail, but also to manage and check address files.

Many of the adjustments in the rate structure have involved the creation of what are commonly referred to as worksharing discounts. (Discounts are used to arrange lower rates for lower-cost mail. They should not be viewed as a means of giving favorable rates to certain mailer groups.)

Giving Mailers More Options

Some postal activities can be done more efficiently by mailers than by the Postal Service. The worksharing notion is to set up a rate structure that gives mailers

choices. If done right, the mailers will choose to do the work only when they do it more efficiently than the Postal Service. For example, suppose it costs the Postal Service four cents per piece to sort mixed mail into three-digit packages. If a presort discount of four cents is given, the mailer will choose to do the sorting only when he can do it for less than four cents.

From the Postal Service's viewpoint, worksharing transfers some of the postal work to the mailer and results in a smaller postal system. It does not affect the Private Express Statutes, since they are interpreted to refer only to the delivery operation. Neither does the universal service obligation. In a real sense, however, it does involve the privatization of large parts of postal work.

From the point of view of the mailer, worksharing results in an increase in overall efficiency, lower postal costs and, as will be explained later, better service. In order to understand the benefits of worksharing, it is helpful to think in terms of several different types of worksharing.

Type 1

The mailer does the work in essentially the same way the Postal Service would do it. In the case of a presort discount, for example, the mailer would create the mailpieces and then sort them either by hand or on a sorting machine. This type of worksharing is one most closely associated with the meaning of the term workshare.

The efficiency gains from this type of worksharing tend to be limited. In the example used above, where the postal cost and the discount are four cents per piece, a mailer ■

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who could do the work for three cents would gain one cent per piece.

Type 2

The mailer achieves the workshared result but does the work differently than the Postal Service would. The best example of a Type-2 situation involves, again, presort discounts. Usually on a computer — although it could be done by hand — the mailer may be able to arrange all of his addresses in ZIP Code order. Then he can print the ZIP Codes, one group after the other.

In a worksharing situation of this kind, the mailer may be able to do the work for a small fraction of what it would cost the Postal Service. Even if he is not using the advanced technology of the computer, and is sorting the addresses by hand, he has the option of doing the work in a completely different way. And, if the same mailing list is used more than once, or is used again with slight modification, he can sort once and do many mailings.

Two features of this kind of situation deserve note. First, the mailer may be able to do in one step what the Postal Service does in two or more steps. Such would be the case if the Postal Service requires two or three sortations to get the mail to the five-digit level, while the computer goes there directly. Second, mailers of considerable volume may be in position to take advantage of this discount without outside help. In fact, unless the outside firm handles a good deal of the mail preparation process, mailers would not be in a position to help in this task at all.

From an efficiency point of view, a Type-2 discount situation is extremely attractive, largely because the potential gains are large. In effect, the potential exists to achieve the sortation without doing the work; but note that if the discount is not offered, none of the benefit will be realized.

Type 3

Here, the mailer's decision is influenced by factors other than the size of the discount and his cost of doing the work. The best example of this situation is when the mailer is concerned about the level or quality of service.

Two examples are important. First, a mailer could find presorted (or barcoded) mail zips through the system without

delay while other mail, which needs more postal attention, is either delayed or is unpredictable. In this situation, the value to the mailer of the added service would be considered along with the cost of doing the work and the size of the discount. (Some mailers have found that turning the mail over to a presort firm, which requires time to do additional work, results in a one-day loss in service. In response, some presort firms provide same-day entry and some drop ship to nearby locations.)

Second, a mailer considering drop shipping could know that mail entered at a destination facility is always delivered within one or two days while that entered at a distant location takes much longer and is less predictable. This mailer would clearly consider the value of the improved service along with the size of the discount and the cost of the drop shipping.

From an efficiency point of view, the situation here also has potential. For example, suppose the discount is four cents per piece and the mailer's cost of doing the work is 3.8 cents. It would seem on first glance that the gain from having the mailer do the work is only 0.2 cents. But if the value of the improved service is one cent per piece, then the gain from offering the discount is amplified to 1.2 cents. If the discount was not offered, the mailer would clearly not do the work or receive the improved service. Also important, is if the improved service is not feasible, the mailer could decide to use an alternative to the postal system. Conversely, the mailer could increase his volume if the discount and the associated service are offered.

Type 4

The mailer reduces the work required by changing his behavior in efficient ways that were either not predicted or did not seem particularly associated with the nature of the discount.

A drop-ship discount, for example, can be as simple as a price for nationwide mail and a price for mail entered at the destination office. A mailer in New York could be sending mail to Los Angeles. If mailed from New York, he would pay the nationwide price, but if entered in Los Angeles, he would pay the lower destination price. If the difference —



between these two prices is large enough, the mailer could hire a trucking firm and drop ship.

There is also the option of having the mail printed by a firm in Los Angeles, which would make destination entry quite natural. Without the drop-ship discount, the mailer will not consider the Los Angeles printer, whose charges might be no higher than the charges of the printer in New York. With the drop-ship discount, the mail might be printed in Los Angeles and the burden of transportation would be avoided entirely.

Consider a variant of the same situation. Suppose a mailer in New York has two mailings going to Los Angeles. If postal prices do not depend on distance, he will print one mailing, enter it in New York and then print the other.

The Postal Service might argue that its costs would be lower if the two mailings were integrated and shipped together. Under these pricing conditions, however, the mailer has no incentive to cooperate in the integration process. But if a drop-ship discount is offered, it is possible that the mailer will integrate the production of the two mailings and ship them more efficiently to their destinations. The savings in transportation from the integration are greater than the cost and bother of doing the integrating, but the mailer will not cooperate under a rate structure without discounts.

As a second example, consider the letter/flat differential. (Some readers may not view a letter/flat rate differential as focused on worksharing. I include it here because it is a discount and it can lead to a reduction in postal work.) Under such a rate structure, letter-size pieces have a lower rate and flat-size pieces have a higher rate. The differential might be justified on the basis of nothing more than an interest in cost-based rates, and worksharing might not be an issue. Some mailers, however, will convert flats into letters. Considering the cost of delivery and the benefits received by the mailer, the letter-size piece might be a more effective piece for the nation as a whole, but the mailer will not make the change unless a rate differential is offered.

Type 5

This situation has worksharing aspects but its primary purpose is to make the postal system more competitive. The drop-ship discount is, again, an obvious example. Suppose a mailer in Cleveland has mail that is to be delivered in Cleveland. If the Postal Service presents him with a rate that does not vary with distance, he will be paying what may amount to a rate based on 1,000 miles of transportation. That is, the average piece of mail goes, say, 1,000 miles, and that is the cost on which the rate is based. Mail going over 1,000 miles gets a relative bargain and mail staying in the office of entry can be viewed as helping to finance the long-distance mail.

Now, suppose there is a private delivery firm in Cleveland that is competing with the Postal Service. The Private Express Statutes in the United States do not prevent private firms from delivering parcels, periodicals, catalogs over 24 pages or saturation mail. They may not, however, use mailboxes. That private firm will base its prices on the costs it experiences, given it both receives and delivers mail in Cleveland — it will not charge a 1,000-mile price. If the Postal Service charges only a 1,000-mile price, with

no distance differentials and associated drop-ship discounts, the Postal Service will on that account be at a disadvantage and may not be competing effectively. It could easily lose business despite being the low-cost carrier.

If the Postal Service offers distance-sensitive prices, it will be more competitive in Cleveland. This is the case whether or not any mailers decide on the basis of the price differentials to engage in drop shipping. In short, the price structure is established in order to be competitive or to base the prices on the actual costs of the mail, and work-sharing activity occurs as a natural result.

Improving the Entire Process

The benefits of offering worksharing discounts clearly go far beyond the extent to which one person can do a particular piece of work cheaper than another person. Once the mailer is given options and the possibility of control, the entire productive operation can be re-planned and the gains range from lower costs to improved service to overall effectiveness in the use of the mail.

It sounds like the rate setting process should be simple — the Postal Service does a cost study and the discount is set equal to the result. In practice, these studies are difficult and often controversial. In addition, some mail costs more for the Postal Service to sort and transport than other mail, and the number of discounts is limited. Also, mailer costs vary. It is often difficult to project demand and assure that the Postal Service will break even. Nevertheless, we have come a long way.

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Workshare Trivia

- About 45% of First-Class Mail is now workshared.
- 43% of Standard A Regular is entered in a destination facility.
- 88% of Standard A Enhanced Carrier Route is entered in a destination facility.
- The total value of all worksharing discounts is nearly \$13 billion. This compares to a total budget of about \$60 billion.