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ORIGINAL

Decision No. 82581

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of UNITED PARCEL SERVICE, INC., for authority to increase certain of its rates for common carrier parcel delivery service.	Application No. 53615 (Filed September 29, 1972; amended October 13, 1972 and January 2, 1973)
And Related Matters.	Case No. 5432, OSH 725 (Filed December 5, 1972) Case No. 5439, OSH 172 Case No. 5441, OSH 259 (Filed December 5, 1972)

Additional Appearances

Rufus G. Thayer, Jr., Attorney at Law, and Edward C. Crawford, for the Commission staff.

FINAL OPINION

Duly noticed public hearings were held in these proceedings February 13, 1973 and June 13, 14, and 15, 1973 before Examiner Thompson at San Francisco. The matters were taken under submission July 8, 1973 on the receipt of late-filed Exhibit 38.

By the application, as amended, United Parcel Service, Inc., a highway common carrier of parcels, seeks authority to establish increases of 3 cents per package and one-half cent per pound in its rates for the transportation of parcels between points in California. By interim order in Decision No. 81692 dated July 31, 1973, applicant was authorized to establish the proposed increase of one-half cent per pound in its parcel rates.

On December 5, 1972, the Commission ordered that hearings be held in Cases Nos. 5432, 5439, and 5441 to be consolidated with hearings in the application for the purpose of determining whether provisions prescribing minimum parcel rates for highway carriers in minimum rate tariffs should be amended to reflect the level of rates established for United Parcel Service, Inc. in this application.

During the 12 months ended September 30, 1972, applicant transported 60,046,476 packages in its intrastate highway common carrier operation. An analysis of applicant's traffic for the past eight years shows a growth and indicates approximately 63 million packages for 1973. Applicant is engaged in expansion of its terminal facilities and anticipates a greater increase in traffic. It estimates that it is possible that as many as 65 million packages may be transported. The proposed 3 cents per package increase in rates would provide additional gross revenues of $1.8 million at the traffic level for the twelve months ended September 30, 1972, $1.89 million at the normal trend growth of 63 million packages, and $1.95 million if traffic growth to 65 million packages is achieved.

Applicant made a number of estimates of the results of operations under the proposed increases in rates. The estimates consider variations in traffic and various circumstances that would affect the level of expenses. All of the estimates, however, are based upon results of the test year of the 12 months ended September 30, 1972. As was stated in Decision No. 81692 applicant performs common carrier operations and contract carrier operations in California intrastate commerce as well as common carrier operations by motor vehicle and by air in interstate commerce in and outside of California. Applicant's equipment, facilities, and personnel in California are utilized in all of its transportation services. A determination of the results of California intrastate highway common carrier operations necessarily requires separations of revenues and separations and allocations of expenses. The methods of separations and formulae for allocations have been developed from discussions between applicant and the Commission staff over a period of years and from decisions of the Commission in prior proceedings.

In Table 1, below, is set forth applicant's estimates of the results of operations for the test period under present rates, adjustments to those results to show results at September 30, 1972 payroll expense and operating tax levels, and adjustments to show the results at the proposed rates at January 1, 1973 payroll and operating tax levels.[1/]

1/ Present rates mean rates in effect September 30, 1972. Proposed rates include the rates at the increases of 1/2 cent per pound authorized in Decision No. 81692 together with the increase of 3 cents per package involved herein.

TABLE 1

Estimated Results of California Intrastate Highway Common Carrier Operations for Twelve Months Ended September 30, 1972 with Adjustments To Reflect Proposed Increased Rates And Payroll Cost Levels as of January 1, 1973

	Test Period Present Rates	Adjusted Test Period Present Rates	Adjusted to 1/1/73 & Proposed Rates
Operating Revenues	$56,278,458	$56,278,458	$61,226,921 1/
Operating Expenses	53,168,394	55,366,800 2/	57,896,637 3/
Net Revenues	$ 3,110,064	$ 911,658	$ 3,330,284
Income Taxes	1,134,237	21,583	1,247,827
Net Income	$ 1,975,827	$ 890,075	$ 2,082,457
Operating Ratios			
Before Taxes	94.47%	98.38%	94.56%
After Taxes	96.49%	98.42%	96.59%

1/	Adjustments for proposed increases in rates:	
	60,046,476 packages @ 3¢ =	$ 1,801,394
	629,413,736 pounds @ 1/2¢ =	3,147,069
	Total adjustment	$ 4,948,463
2/	Adjustments to reflect wages and fringe benefits and payroll tax rates in effect September 30, 1972 for full period	$ 2,176,299
	Adjustment to reflect state gasoline sales tax	22,107
	Total expense adjustments for 9/30/72	$ 2,198,406
3/	Adjustments to reflect wage, fringe benefits and payroll tax rates effective January 1, 1973	$ 2,814,944
	Adjustments to eliminate California State Transportation Tax and to add additional gross receipts taxes on increased revenue	$ (285,107)
	Total expense adjustments for 1/1/73	$ 2,529,837

On the basis of the results shown in Table 1, applicant forecast the results of operations for a year ending December 31, 1973. Applicant's highway common carrier traffic has had a growth rate of about 4.9 percent per annum. It has recently expanded its interstate air parcel service and it has engaged in a program of expanding and improving terminal facilities in California which is estimated will cost $7.5 million in 1973 for buildings and equipment. It anticipates, and hopes, to increase the rate of its growth of traffic so as to obtain 65 million packages for California intrastate highway common carrier transportation during 1973. That would be an increase of 8.25 percent over that for the twelve months ended September 30, 1972, whereas the increase for 15 months at the normal trend would be about 6.1 percent.

In making its projections for gross revenue which would be received from the transportation of 65 million packages applicant divided the estimated gross revenue at the proposed rates shown on Table 1 ($61,226,921) by the number of packages transported during the test period (60,046,476) to obtain an average revenue per package ($1.0197), and applied that average to 65 million packages.

In projecting its expenses it first separated the expenses for the test period into the three categories of (1) payroll related expense, (2) nonpayroll expense, and (3) business service expense. The payroll related expense was estimated by applying the wage rates, fringe benefits, and payroll tax rates effective January 1, 1973 for southern California employees to the test period operations, and applying the wage rates, and fringe benefits effective January 1, 1973 for northern California employees to the first six months of the test period and those wage rates and fringe benefits increased by 6.2 percent for the second six months of the test period and applied the payroll taxes at the rates effective January 1, 1973.[2/] The sum of the payroll costs so determined was divided by the number of packages for the test period. The quotient was reduced by 0.24 percent to reflect increased productivity gains and the resulting factor was applied to 65 million packages.

In projecting the nonpayroll expense applicant divided the amount for the test period by the number of packages for the test period, increased the quotient by 5.88 percent which is the average increase in nonpayroll expense experienced by applicant over the past five years, and applied the resulting factor to 65 million packages.

Business service expense relates to services for which applicant pays fees to the parent company. Applicant estimated that expense pursuant to the method for assigning costs based upon underlying expenses rather than upon the fees paid or payable to the parent company.

2/ That procedure underestimates the payroll related costs that can reasonably be anticipated because the January 1, 1973 collective bargaining agreement with southern California employees expired October 30, 1973 and Exhibit 38 shows that the package offered by applicant in negotiations with its northern California employees for a new collective bargaining agreement to become effective July 1, 1973 calls for a 7.2 percent increase in the cost of wages and fringe benefits rather than the 6.2 percent increase used in the estimate.

The validity of the estimates of applicant rests mainly upon the 0.24 percent and 5.88 percent increase factors it applied. Those figures represent the average of the increases per year over the past five years experienced by applicant. Applicant's analysis of productivity gains is set forth in Exhibit 22. For each of the various work functions (pickup, sorting, feeder, delivery, office, and shop) is set forth for each year, 1968 through 1972, the number of package handlings and the man-hours. The man-hours per 1,000 package handlings for each function were weighted by the percentage of man-hours required for each function and of the total thereof divided into 1,000 provided the weighted packages per total man-hour for each year. The results so shown are set forth below in Table 3.

TABLE 3

Average Annual Gain in Productivity
1968 - 1972

	1968	1969	1970	1971	1972
Total Man-hours	6,438,534	6,747,362	7,067,188	7,134,182	7,816,734
Packages Per Man-hour (Weighted)	32.84	32.89	32.47	32.44	33.15
% Increase over Previous Year		.15	(1.28)	(.09)	2.19
Packages Billed In California *	78,766,412	82,081,147	82,796,812	84,780,228	92,831,595

* These figures do not represent the number of handlings for each function. Some packages delivered in California and originating outside the State are not billed in California, and some packages billed in California receive more than one sorting.

The estimated 0.24 percent productivity gain represents an average of the percentage increases over previous years [.15 + (1.28) + (.09) + 2.99]. The average so determined has little validity as representing any trend of gains or losses in productivity. Indeed, the figures shown for packages per man-hour (weighted) do not indicate any trend at all. The most that can be said of Table 3 is that it indicates that with the greater than usual increase of packages billed in California in 1972 over 1971 there was a productivity gain of 2.19 percent. An analysis of the data in Exhibit 22 discloses that there is no indication of any kind of trend of productivity over the five year period with respect to any of the work functions. Some inferences can be drawn from a comparison of the data for 1972 with similar data for 1971. Table 4, below, compares the increases in packages handled and man-hours by work function of 1972 over 1971.

TABLE 4

Percentages of Increases in Packages Handled And Man-Hours by Work Function 1972 Over 1971

Work Function	Packages Handled	Man-Hours
Pickup	6.95	7.66
Central Sorting	11.44	12.01
Feeder	12.09	11.72
Delivery	11.05	10.86
Office	10.95*	10.47
Shop	10.95*	10.17

* Number of packages billed in California.

The fact that the increase in packages handled in pickup service is so much less than the increases in packages billed and package handlings in the delivery function indicates that much of the increase in packages billed in California was due to an increase in interstate traffic moving into California. The testimony that applicant has expanded its air parcel service corroborates that inference. A comparison of the figures shown for central sorting, feeder, and delivery functions provides a reasonable inference that the nature of applicant's operation is such that a substantial increase in traffic requires a greater increase in the utilization of manpower in the central sorting function than required for the feeder and delivery functions. The importance of this from a cost standpoint becomes apparent from the fact that in 1971 central sorting required 12.46 percent of total man-hours and 13.66 in 1972, whereas in 1971 the feeder and delivery functions required 58.78 percent of the total man-hours and only 58.70 hours in 1972, reflecting a shift of man-hours from feeder and delivery function to central sorting. The labor costs per hour of employees engaged in the different functions are not of record. From our experience in other proceedings involving labor costs per hour of drivers and terminal employees at wage rates provided in contracts with the Brotherhood of Teamsters,we are of the opinion that the labor cost per man-hour in the sorting function would be less than that for the delivery and feeder functions.

Table 4 also corroborates other evidence showing that not only payroll costs but also nonpayroll costs are variable with traffic. Certainly increases in equipment, facilities, and supplies are required to implement an increase in work force of over 10 percent.

The 5.88 percent average annual increase in nonpayroll expense was taken from data in Exhibit 23 which is summarized below.

TABLE 5

United Parcel Service, Inc., California Districts

Increase Per Package in Nonpayroll Expense
(Excluding Business Service Fee)
12 Months Ended September 30
1968 through 1972

	1968	1969	1970	1971	1972
Packages billed in California (000)*	78,766	82,081	82,797	84,780	92,832
% Increase		4.21%	.87%	2.40%	9.50%
Nonpayroll Expense (000)	$13,495	$15,221	$15,953	$17,124	$19,982
Nonpayroll Expense Per Package (cents)	17.13	18.54	19.26	20.19	21.52
Percent Increase Over Previous Year		8.23%	3.88%	4.83%	6.59%

* Exact number of billings in California (interstate and intrastate) is shown in Table 3.

The 5.88 percent figure is an average of the percent figures shown on the bottom line. The data shows that there has been a continuing increase in nonpayroll expense and that nonpayroll expense varies with the amount of traffic.

With respect to applicant's contention that nonpayroll costs as well as payroll costs increase with the amount of traffic handled, the evidence shows that such is the case. Its contention that nonpayroll expenses per package have also increased annually has also been shown. Applicant's estimate of an annual increase of 5.88 percent appears to be reasonable. It is common knowledge that costs of construction, equipment, supplies, and services have been increasing and applicant's estimate reasonably reflects the trend. With respect to its contention that the application of a .24 percent productivity gain in ascertaining the average labor cost per package will reasonably project payroll costs for the handling of 65 million packages, we do not agree. First of all, Table 3 shows that with a substantial gain in traffic (9.5 percent) there was a gain in overall production per man-hour (2.19 percent). Applicant estimates a substantial gain in California intrastate traffic. Secondly, Table 4 indicates that with the substantial gain in traffic applicant has been able to shift the man-hours required from functions having a higher labor cost per hour to a function with a lower labor cost per hour. If all other factors remained constant that factor would reduce its labor cost per package which is one measure of productivity gain. That circumstance is supported by evidence that applicant planned construction in 1973 of new terminal facilities at five locations in California, and it is estimated that the cost of the buildings and equipment will be approximately $7.3 million. In terms of gross revenue, applicant is the largest highway common carrier in California. It is and has been able to provide an insured parcel delivery service at rates lower than the uninsured parcel post service of the United States Postal Service and has done so at a profit. In the light of its demonstrated business acumen it would be difficult to believe that applicant would undertake that capital expenditure in terminal facilities unless it anticipated that by doing so it would increase its efficiency. We are of the opinion that for the purpose of projecting payroll costs for the year ended December 31, 1973 the payroll cost per package should be reduced by 2 percent to reflect the aforementioned productivity gains.

Table 6, below, sets forth applicant's estimate together with the estimate adjusted to reflect the 2 percent gain.

TABLE 6

Estimated Result of California
Intrastate Highway Common Carrier
Operations of United Parcel Service
For the Year 1973 at Proposed Rates

	Table 1	Applicant's Estimate	Adjusted Estimate
No. Packages	60,046,476	65,000,000	65,000,000
Operating Revenues	$61,226,921	$66,280,500	$66,280,500
Operating Expense			
Payroll	$43,793,202	$47,866,000	$47,039,000
Nonpayroll	12,383,708	14,202,500	14,202,500
Bus. Service	1,719,727	1,880,676	1,880,500
Total Expense	$57,896,637	$63,949,176	$63,122,000
Net Revenues	$ 3,330,284	$ 2,331,324	$ 3,158,500
Income Taxes			
State	$ 222,903	$ 132,177	$ 201,946
Federal	1,024,924	520,845	907,283
Total Taxes	$ 1,247,827	$ 653,022	$ 1,109,229
Net Income	$ 2,082,457	$ 1,678,302	$ 2,049,271
Operating Ratio			
Before Income Tax	94.56%	96.48%	95.23%
After Income Tax	96.59%	97.47%	96.91%
Rate of Return	11.7%	8.1%	9.85%
Rate Base			
Properties as of:	9/30/72	3/31/73	3/31/73
Depreciated Value	$15,566,828	$17,566,665	$17,566,665
Working Capital	2,959,385	3,266,215	3,232,018
Total	$18,526,213	$20,832,880	$20,798,683

The Table 1 expense estimates are underestimates in that they do not consider increases in wages and fringe benefits effective during 1973. If those were included, the results for transporting 60,046,476 packages would reflect an operating loss. Applicant's estimate and the adjusted estimate of expense for the transportation of 65,000,000 packages are also understated to the extent that only a 6.2 percent increase in wages and fringe benefits for northern California employees are considered, whereas Exhibit 38 shows that the effective increase is at least 7.2 percent; and the payroll estimates do not project any increase in wages and fringe benefits for southern California employees during 1973 even though the collective bargaining agreement with those employees terminated October 30, 1973.

The Commission staff presented an estimate of earnings of applicant at the proposed rate for the calendar year 1973. Basically that estimate corresponds to applicant's estimate except that increases in nonpayroll expenses were not projected and the depreciation of vehicles and plant equipment was based upon service lives almost double that utilized by applicant. Applicant based its estimates upon the service lives and rates of depreciation heretofore approved by the Commission. The increase in service lives estimated by the staff has no support from any competent evidence in this record. The projection of nonpayroll expense estimated by applicant is supported by the record.

In Decision No. 78811 dated June 22, 1971 in Application No. 52362, the Commission stated,

> "...we reach the ultimate finding that a rate of return within the range heretofore granted to UPS of 10.4 to 12.0 percent will be reasonable herein."

There is nothing in the present record which would support a different finding.

Keeping in mind that the adjusted results shown in Table 6 are predicated upon underestimates of payroll expenses as well as the fact that the estimated revenues are based upon an increase in traffic in excess of applicant's normal growth, the earnings of applicant at the proposed rates on California intrastate highway common carrier transportation will not be excessive.

In prior proceedings the Commission has found that applicant is the rate-making carrier for the transportation of parcels from wholesalers and jobbers, and more particularly for transportation for which minimum rates are prescribed in Item 265 of Minimum Rate Tariff 2, Item 850 of Minimum Rate Tariff 1-B, Item 420 of Minimum Rate Tariff 9-B, and Item 425 of Minimum Rate Tariff 19. The Commission staff recommends that the aforementioned minimum rate tariff items should be amended so as to conform with whatever rates the Commission may authorize applicant. The minimum rates named in those items were established to authorize highway carriers to meet the going rates of United Parcel Service, Inc. in order to afford them equal opportunity to compete. There was no opposition to the staff's recommendation. It should be adopted.

We find that:

1. United Parcel Service, Inc. is a highway common carrier of parcels sold at wholesale. It here seeks authority to increase rates for its highway common carrier service by three cents per package and by one-half cent per pound.

2. Duly noticed public hearings were held in this application at which all persons and parties were accorded full opportunity to participate therein.

3. For the test year ending December 31, 1973 applicant will conduct its highway common carrier operations at a loss at present rates. Assuming an increase of 8.25 percent in traffic over that experienced for the twelve months ended September 30, 1972, the proposed increase of three cents per package will provide applicant additional gross revenues of $1,950,000, and the proposed increase of one-half cent per pound will provide additional gross revenue of $3,406,700, for a total of $5,356,700, or an increase of 8.8 percent.

4. The increased traffic and the increased rates will permit applicant to earn from its highway common carrier operations a rate of return not in excess of 9.85 percent, and will provide it with an operating ratio not more favorable than 96.91 percent, which results are reasonable.

5. The rate increase is cost-justified and does not reflect future inflationary expectations.

6. The increase is the minimum required to assure continued adequate and safe service.

7. The rate increase will achieve the minimum rate of return and the maximum operating ratio needed to attract capital at reasonable costs and not to impair the credit of the carrier.

8. The rate increase takes into account expected and obtainable productivity gains.

9. The rates resulting from the proposed increase are lower than the rates for parcel post between the same points in California.

10. The proposed rate increase has been shown to be justified.

11. The rates of applicant have heretofore been adopted and approved as minimum rates for parcel delivery service by highway carriers.

We conclude that applicant should be authorized to establish the proposed increase in rates on not less than five days' notice, that Minimum Rate Tariffs 1-B, 2, 9-B, and 19 should be amended by separate order to reflect the proposed wholesale parcel delivery rates, and that common carriers now maintaining parcel delivery rates comparable to the rates of applicant but otherwise lower than the established minimum rates should be authorized and directed to increase such rates so as to preserve competitive relationships.

FINAL ORDER

IT IS ORDERED that:

1. United Parcel Service, Inc. is authorized to establish the following increased rates and charges:

Amend Item 150-A of Local Parcel Tariff Cal. P.U.C. No. 18 by canceling paragraphs (a) and (b) of said item and substituting therefor the following paragraphs:

(a) The rate for packages moving wholly within Territory A, wholly within Territory B, or wholly within Territory C, as described in Item 25, shall be 42 cents per package plus 4 cents for each pound or fraction thereof of its weight.

(b) The rates for all packages, except packages covered by paragraph (a) above, shall be 42 cents per package plus the following rates for each pound or fraction thereof of its weight.

Zone	Rate Per Pound or Fraction Thereof
2	5¢
3	6¢
4	8¢
5	10¢

(To determine the applicable zone between any two California points, consult governing publication referred to in Item 10 hereof.)

2. Tariff publications authorized to be made as a result of the order herein may be made effective not earlier than five days after the effective date of this order on not less than five days' notice to the Commission and to the public.

3. The authority hereinabove granted shall expire unless exercised within ninety days after the effective date of this order.

4. Common carriers maintaining, under outstanding authorizations permitting the alternative use of common carrier rates, parcel delivery rates comparable to the rates maintained by United Parcel Service, Inc., but otherwise less than the minimum rates established by the Commission applicable thereto, are authorized and directed to increase such rates to the level of the rates authorized in paragraph 1 hereof, or to the level of the minimum rates specified and established in the Commission's minimum rate tariffs, whichever is the lower. Tariff publications authorized and required to be made by common carriers as a result of the order herein may be made effective not earlier than the fifth day after the effective date of this order, on not less than five days' notice to the Commission and to the public, and shall be made effective not later than thirty days after the effective date of the tariff publications made pursuant to the authority granted in Ordering Paragraph 1.

5. Common carriers, in establishing and maintaining the rates authorized hereinabove, are hereby authorized to depart from the provisions of Section 460 of the Public Utilities Code to the extent necessary to adjust long- and short-haul departures now maintained under outstanding authorizations; such outstanding authorizations are hereby modified only to the extent necessary to comply with this order;

and schedules containing the rates published under this authority shall make reference to the prior orders authorizing long- and short-haul departures and to this order.

The effective date of this order shall be ten days after the date hereof.

Dated at San Francisco, California, this 12th day of MARCH, 1974.

Vernon L. Sturgeon
President

William Symons, Jr.

J. P. Vukasin, Jr.

[illegible]

Commissioners

Commissioner Thomas Moran, being necessarily absent, did not participate in the disposition of this proceeding.