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STATEMENT

OF

DAVID R. ROSS
PRESIDENT,
AIRLINE PROFESSIONALS ASSOCIATION, TEAMSTERS LOCAL 1224

BEFORE THE

COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE
U.S. HOUSE OF REPRESENTATIVES

ENTITLED

"EFFECTS OF PROPOSED ARRANGEMENT BETWEEN DHL AND UPS ON COMPETITION, CUSTOMER SERVICE, AND EMPLOYMENT"

PRESENTED ON

SEPTEMBER 16, 2008

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President
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Mr. Chairman, Ranking Member Mica, and Members of the Committee, I am grateful you have called this hearing because this issue is so terribly important to our national economy and so many workers in Ohio, around the country, and in our transportation industry. Proof of that, is you have called this hearing. Further proof of that, is I have had the distinct privilege of personally briefing both Presidential candidates in this election, Senator Barack Obama and Senator John McCain. I have personally heard them express their concerns about the antitrust issues and job losses generated by this anticompetitive deal between UPS and DHL. As you know, Mr. Chairman, Senator Obama wrote the White House and Senator McCain wrote the Antitrust Subcommittee in the United States Senate, both expressing their concerns about the concentrated job losses associated with and the anticompetitive nature of this deal. At a hearing last week before the House Judiciary Committee, Chairman John Conyers, Jr. concluded more hearings were required to properly address the antitrust implications of this proposed deal and the impact on competition in the air shipping industry.

Mr. Chairman, I respectfully request that this Committee (1) oppose the deal between DHL and UPS as an affront to U.S. aviation policy, which seeks to promote competition in the air transportation industry and discourage excessive market domination;[1] (2) request that this Justice Department initiate an investigation and enforce

[1] See 49 U.S.C. §§ 40101(a)(6), (9), (10), (b), and (f).

the antitrust laws of this country in defense of America's aviation industry; and (3) resist any attempts to grant DHL a waiver of the citizenship laws that keep our country safe and ensure the fair application of our labor laws.

My name is Dave Ross, and I am a Captain with ABX Air. I am also the President of Teamsters Local 1224 that represents pilots who fly for ABX Air. I graduated from the United States Air Force Academy in 1983, I flew as an instructor and an evaluator in the T-37 and B-52, and I flew in Desert Storm where I was awarded two Air Medals and the Distinguished Flying Cross. I only mention my military credentials because I want to emphasize that I am proud of my service and defense of our American way of life. Mr. Chairman and members of the Committee, thank you for inviting me to testify before you about the strategic global alliance between two dominant air express carriers – DHL and UPS. This deal, if allowed, would have serious negative effects on service, costs, consumer choice and jobs.

DHL's restructuring announcement threatens the careers of our members and their ability to provide for their families. As the President of Teamsters Local 1224, with the support of the International Brotherhood of Teamsters, I testify before you on their behalf. Also, I am here to speak about a potential economic crisis that threatens a small town in Ohio called Wilmington. This pending economic crisis was brought about by two global corporate giants who seek to merge their services and destroy competition as we know it in the air express market. Through mismanagement, DHL is losing money in the U.S. Their proposed deal with UPS violates antitrust laws and is an affront to U.S. aviation policy. Rather than fix their management problems, DHL is now trying to circumvent our antitrust laws and undermine our aviation policies. Mismanagement of

the business is no excuse to violate our antitrust laws and undermine our aviation policies.

Airborne Express was acquired by and then greatly controlled by DHL

You probably remember our airline as Airborne Express. Airborne Express entered the express delivery business in the forties, delivering tropical flowers from Hawaii. Airborne rapidly expanded with a domestic focus while serving the shipping needs of business customers and specialty services. Airborne purchased Clinton County Air Force Base in 1980, and developed it as the Wilmington Air Park. While enjoying a relatively low cost structure, Airborne was a consistent third competitor in the domestic express delivery market that offered a lower priced alternative to consumers and small businesses.

Airborne Express and DHL had reciprocal strengths. While Airborne established itself as a strong competitor in the U.S., DHL dominated the international market. DHL began in California, and even though they were strong internationally, they represented only a small share of the U.S. market. Deutsche Post World Net invested in DHL, and gradually increased their investment until gaining 100% ownership in 2002. Soon thereafter, DHL purchased Airborne Express promising to increase market shares and profitability of both partners, improve services for consumers, and increase competition. At the time of the purchase, Deutsche Post rightfully praised the complimentary service portfolios of the two airlines and Airborne's broad ground network. By every measure, this was an acquisition that should have increased competition thereby benefiting consumers and creating jobs.

After the purchase, DHL operated two airlines in the U.S. – Airborne Express and DHL Airways. In Europe, DHL operates two airlines – European Air Transport based in Brussels and DHL Air UK based in East Midlands. Accordingly, any suggestion they can't operate successfully in the U.S. with two airlines is contradicted by their operations elsewhere. DHL also operates DHL Middle East based at Bahrain and DHL Latin American based in Panama City. More recently, DHL announced plans to forge an alliance – a joint venture – between it and Lufthansa Cargo called AeroLogic, with each having a fifty percent share and flying cargo from a new sort hub at Leipzig/Halle airport. The opening ceremony for that hub was on May 26th and was attended by the Mayor of Wilmington, Ohio. That was two days before DHL's announcement that devastated Wilmington, Ohio.

As this Committee is surely aware, DHL's entry into the U.S. market triggered a lengthy proceeding before the Department of Transportation because of well-established citizenship laws for U.S. air carriers. In 2003, Administrative Law Judge Burton S. Kolko declared DHL Airways a U.S. citizen in DOT Docket Proceeding Number OST-2002-13089-594. Around that time, the two airlines carrying express packages for DHL were renamed. Airborne Express became ABX while operating at the Wilmington Airport, and DHL Airways become Astar while operating sixty miles away at the Cincinnati/Kentucky International Airport. There was an attempt to relax the citizenship and control laws in a Notice of Proposed Rulemaking and a Supplemental Notice of Proposed Rulemaking (Docket Number OST-2003-15759), which was withdrawn after Congress rejected it in a bipartisan manner.

DHL, however, exercised great control over ABX and Astar through two separate long-term contracts called ACMI Agreements whereby the airlines provide services for aircraft, crew, maintenance and insurance. Through these ACMI Agreements, DHL controlled the routes, the on-time performance criteria, third party services, and any changes of ownership in the form of changes of control. The two airlines provided express delivery service on a cost plus basis, with ABX reimbursed for all expenses plus a base markup of 1.75% of revenues and an incentive for performance which could increase the markup to 2.5%. ABX also has a Hub Services contract with DHL to operate the sort center in Wilmington and other regional sort hubs.

Through the considerable control exercised by DHL, service declined and market share suffered. While DHL proposes this alliance with UPS because of cost problems, the reality is they've created a revenue problem because they mismanaged the business.

DHL's declining market share in a growing market

In the air express business, on-time-performance is everything. At the time DHL purchased Airborne Express, Airborne had an 18.4% share of the market. From 2003 to 2007, with DHL in control, rather than realizing the synergies and complimentary strengths of Airborne and DHL International, service declined. Accordingly, package volumes declined. Market share at DHL/Airborne declined more than 25%, while FedEx and UPS gained 10.3% and 11.2% respectively. A catastrophic service failure occurred in September 2005, when DHL mismanaged combining the two sort facilities into one at the Wilmington Air Park. Rather than integrate the sort facilities over time, they tried to do it in one night. In a service industry like this, where on-time-performance is measured in tenths of percentage points, on-time-performance dropped below 70% and did not

recover for months[2] because of decisions made by DHL managers and the effective control they exercised through contractual Agreements.

While Deutsche Post spoke of increased competition and expanded service when they purchased Airborne Express, the reality is service declined and they now propose to no longer compete. As a result, competition itself is threatened in the express package delivery business. When on-time-performance declined, market share declined. Market share for the dominant players, one brown and the other purple, increased commensurately. While problems arose with the consolidation, DHL continued their managerial pursuits with unswerving determination but negative results. They operated two airlines, with two divergent CEO's, two middle management structures, two airline support structures, and two very different aircraft fleets. They created havoc resulting in a revenue problem caused by mismanagement through the control they exercised, resulting in a loss of market share. DHL lost market share in a growing market that, last year, set an industry revenue record at $32.81 billion.[3]

Fuel-efficient Boeing 767's, but dysfunctional corporate relationship

At ABX, we fly more than forty fuel-efficient Boeing 767 aircraft that have Category II and III capability which allows us to land in nearly all weather conditions. ABX has an established history of delivering high margin express packages for the lowest cost with impeccable reliability. DHL has expressed concern that some of our

[2] "Development of the U.S. Air Express Market (2003-2007)", Air Cargo Management Group (Aug. 15, 2008) (ACMG Report), at 13 and 14.

[3] ACMG Report, at 1, 6, 13, and 14.

aircraft are equipped to handle packages in "C" containers rather than "A" containers.[4] First and foremost, express delivery customers are concerned with consistent on-time-performance. Second, some customers specifically request "C" container handling to ensure security of high-value shipments. Third, FedEx recently deployed a "Micro A" container which is essentially six "C"-like containers that are fastened together before loading to realize the benefits of the "C" container. Our system benefited in through-sort capability by using the smaller container, and provided more security and breakage protection.

Friction between senior management at DHL and ABX publicly surfaced when DHL withheld a pre-payment of about $9 million to ABX under the ACMI Agreement because they believed ABX was exceeding a 10% revenue threshold from non-DHL customers and demanded reallocation of overhead expenses related to non-DHL business. ABX declared DHL in default. Before that, Astar CEO John Dasburg attempted to acquire ABX for $7.75 per share in August 2007, but ABX CEO Joe Hete rejected the offer without a counter-offer and with minimal, if any, rationale. On the last day of 2007, ABX acquired two airlines made up largely of old and fuel-inefficient aircraft for $332 million and created a holding company, Air Transport Services Group, of which ABX is now under. DHL demanded full repayment for a $90 million note because of a change of control at ABX. Today, ATSG stock is valued at a small fraction of its worth at the time DHL purchased Airborne Express and ABX shareholders have suffered. The relationship between DHL, ABX and Astar involves conflicting corporate egos, clashing cultures, and

[4] While "A" containers are shaped like the letter "A" and fill the width of an aircraft fuselage, "C" containers are shaped like the letter "C" and fill about half the width of an aircraft fuselage. Both have their advantages and disadvantages.

inconceivable blunders that have brought great pain to employees and surrounding communities. Yet, nobody has taken responsibility for the failures that have occurred.

Airborne Express was a profitable company that never had a losing year and only one losing quarter. How can a thriving global corporation such as Deutsche Post World Net turn such a consistently competitive company into a venture they now claim stands to lose more than 1 billion dollars a year, while themselves, made pre-tax profit of more than 3.2 billion euros last year and more than 3.8 billion euros the year before that?

Service reductions and job losses

DHL sorts a significant amount of their express delivery packages at regional sort hubs, in cities such as Erie, Pennsylvania; Chehalis, Washington; Waco, Texas; and Memphis, Tennessee. There are more than five hundred jobs at risk in these areas. Also, small businesses who conveniently locate themselves near these regional sort hubs will suffer when DHL withdraws service at these areas, which they surely will. Five hundred jobs are at risk in Riverside, California where DHL operates at March Air Reserve Base. March GlobalPort was formed to coordinate companies that conveniently operate nearby, an area where federal funds were granted to facilitate business. The impacts of this proposed deal extend far beyond Ohio. DHL's withdrawal from these regional sort facilities, which will inevitably occur if this merging of services is allowed, will adversely affect businesses that have set up their infrastructure for supply and delivery of products that depend on a competitive and responsive domestic express delivery business. Service also suffered.

Since their restructuring announcement, according to the dhl-usa web-site, the earliest DHL can deliver express packages at many locations is 5 pm. For more remote

areas, the fastest DHL now offers "DHL Next Day" service is one week. The earliest DHL can deliver an express package from D.C. to a district office in Duluth, Minnesota is 5 pm. For Chisholm, that "express" package will take two days to arrive. For Brainerd, it will take almost a week. DHL is no longer competitive in West Virginia either. The earliest DHL can deliver an express package from D.C. to a district office in Bluefield, West Virginia is 5 pm. For Beckley, that "express" package will take almost a week to arrive. The type of service DHL offers since their restructuring announcement is no longer competitive in the air express market and consumers are responding appropriately. If this trend continues, consumers and small businesses will be left with only two viable choices since the market will be 96% dominated by a duopoly comprised of FedEx and a constructively merged UPS-DHL. Specialty services, such as a very late pick-up for a cancer treatment drug maker who shipped out of Nashville and a very early delivery for a drug testing company in Kansas City, are being lost. Wal-Mart announced they ended their agreement with DHL from their jewelry division because DHL changed their flight route patterns.

Antitrust concerns and our national transportation policy

The anti-competitive nature of this strategic alliance was addressed at length last week. Antitrust expert David Bolto reviewed the circumstances of this deal and testified:

> Dressing up this arrangement as a so-called alliance does not diminish its substantial potential anticompetitive effects. Having DHL depend on UPS for its most critical functions will extinguish rivalry and greatly enhance the likelihood of higher prices and weaker service. Millions of consumers will suffer.

If this third competitor in the air express market is lost, competition in the air express industry will be gone forever and the express package delivery market will be

permanently changed. Antitrust laws exist to ensure competition in the free market system. They prohibit anticompetitive behavior, monopolies, and unfair business practices. As an operator in the express delivery business for more than sixteen years, there are two important things I have observed. First, impeccable on-time-performance is nearly everything in this business. Second, competition in this business is good. FedEx and UPS are fierce competitors, and without a reliable third consumer choice they would no longer have to contend with pricing pressure. The total revenue for the U.S. air freight and express industry was more than $32 billion last year, an industry record. The two industry giants, FedEx and UPS, continue to advertise strongly for express delivery customers. In a letter to the U.S. Justice Department, the Chair and Ranking Member of the Senate Judiciary Subcommittee on Antitrust, neither of whom are from Ohio, have said there may be antitrust issues raised by the proposed deal between DHL and UPS, and we agree. According to Mergers & Acquisitions Report, FedEx backed out of a deal with Deutsche Post earlier this year because of antitrust concerns.[5]

A key element of the express delivery business is package tracking. It is the backbone of this service process. By combining efforts in this process, DHL and UPS will be sharing highly sensitive proprietary information that would normally be closely guarded by real competitors. Even if barriers to information sharing could be erected, the temptation for collusion would be too risky for consumers. A critical element of express package delivery is scanning the bar code. Once the bar code is scanned, an incredible amount of secret proprietary information is exchanged between the different segments of service – from pick-up, to final delivery. Having watched express packages go through the sort for sixteen years, and being in constant contact with the people doing the sorting,

[5] "FedEx Eyeing Deal to Buy DHL", Ken MacFadyen, Mergers & Acquisitions Report, Feb. 4, 2008.

I am here to tell you – there is no way UPS can sort and deliver DHL packages without material commercial proprietary information being transmitted to UPS. True competitors erect every guard possible against exposing such sensitive proprietary information from the public, and now DHL proposes to make it freely available to a supposed competitor.

While a technological "Chinese wall" may be developed to guard against information sharing, the same technology may be used to look over, around, or through that wall. A Chinese wall as a self-regulatory safeguard can hardly be sufficient to secure competitively sensitive information. It would require constant monitoring and the threat of enforcement action, it would have to ensure pertinent information was shared, and it would destroy the very efficiency the strategic alliance was designed to generate.

From a notional view, it makes no sense to rely on a major competitor for a key element of your service, especially in such a consolidated marketplace. Unfortunately, DHL and UPS announced this far-ranging deal even though the terms of the deal were not yet agreed upon. It defies belief that a competitive choice will be available, even to DHL, when the ten year proposed contract with UPS ends. A deal like this would leave the UPS-DHL strategic alliance with 54% of the express delivery market and FedEx with 42% of the market; resulting in a monster duopoly having a combined market share of 96%.[6] This will eliminate competition in this consolidated industry that supports thousands of small business and millions of consumers across America – perhaps forever. When considering the size and ferocity of the competition, and the long-term capital investment required for an airline, the FAA and other licensing requirements, and many other barriers to entry, stopping this anticompetitive deal is the last chance for three competitors in the U.S. air express market. Another potential harm is to the Civil Reserve

[6] ACMG Report, Figs 4-2 and 5-1.

Air Fleet. ABX has seventeen fuel-efficient Boeing 767's dedicated to the Civil Reserve Air Fleet, and Astar has another seventeen aircraft so dedicated, which could be lost if this deal goes through.

These two global giants will no longer compete in the U.S., and even if they do compete internationally, it will be of no benefit to American consumers. It seems these global giants are already colluding in their denials, with one saying "there are no grounds for the candidates' demands for an antitrust investigation"[7], and the other saying "[i]t's a little surprising that anybody could realistically look at this and argue that it raises antitrust issues."[8] The antitrust and competition issues raised by the proposed deal between DHL and UPS are not politics, but real, as shown by the letter from Senators Kohl and Hatch.

Beyond traditional antitrust requirements, our national transportation policy calls for "avoiding unreasonable industry concentration, excessive market domination, monopoly powers, and other conditions that would tend to allow at least one air carrier or foreign air carrier unreasonably to increase prices, reduce services, or exclude competition in air transportation."[9] Our stated national policy further calls for "placing maximum reliance on competitive market forces and on actual and potential

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[7] Dr. Frank Appel, CEO of Deutsche Post AG (Wall Street Journal, Aug. 14, 2008).

[8] Norman Black, UPS spokesman (Wall Street Journal, Aug. 8, 2008).

[9] 49 U.S.C. § 40101(a)(10).

competition"[10] and "preventing unfair, deceptive, predatory, or anticompetitive practices in air transportation."[11]

Something else going on?

One justification given by this extremely profitable global corporation for their restructuring is the foreign ownership restrictions in the U.S. I would stress to you it is doubtful Deutsche Post and DHL Express would have done anything differently if they had 51.1% or greater ownership interest in Astar rather than the 49% ownership interest they have. The ACMI agreements give DHL everything it needs to run a profitable express package delivery airline – control of routes, schedules, on-time performance criteria, third-party services, any changes of ownership.

Moreover, the foreign ownership or nationality requirements play a crucial role in America's security and other national interests. I feel particularly compelled to mention this in light of a suggestion last week that DHL be granted a waiver of these requirements. As became tragically apparent in 2001, after fanatics decided to use airplanes as their weapon of choice, the airline business is different from other industries when it comes to national security. The airline industry also has unique labor concerns because of the mobile labor dynamic involved. The nationality requirements allow our labor laws to be properly applied, and are therefore an important part of carrying out our stated policy goal of "encouraging fair wages and working conditions."[12] Nationality laws further ensure our passenger and cargo airlines are fully available to the Civil

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[10] 49 U.S.C. § 40101(a)(6).

[11] 49 U.S.C. §40101(a)(9).

[12] 49 U.S.C. § 40101(a)(5).

Reserve Air Fleet (CRAF) to fulfill the unique interrelationship between civil and military flying.

As a result of the DHL Airways Citizenship proceeding in 2003, a foreign entity was granted more control over a U.S. air carrier than had ever been granted before. Indeed, through changing Airborne Express to ABX Air, corporate shell games, acquisitions, holding restructurings, and other corporate machinations, the result is the slow cessation of a third competitor in the domestic express delivery market, that previously, had never had a losing year.

Air transportation negotiators from the U.S. State Department mention job growth promised from an academic analysis, by the European Commission and performed by Booz Allen Hamilton, to support greater liberalization in air transport agreements.[13] This Report calls for the creation of an Open Aviation Area. Specific to DHL operations in the U.S., this report suggests DHL should be allowed to operate its own cabotage services that would allow fleet efficiencies and economies of scale, thus reducing costs. DHL's losses in the U.S. market were self-inflicted because they mismanaged the business and lost revenue even though it continues to enjoy profits internationally. But while the Booz Allen Hamilton Report makes an excuse for DHL's financial hardships, citing U.S. citizenship rules, it views the UPS hub at Cologne-Bonn favorably.

The Europeans want access to the American market, either directly through cabotage or indirectly through control. The argument by some that they perceive asymmetrical access is not reality. U.S. air carriers cannot fly passengers from London to Edinburgh just as

[13] Booz Allen Hamilton Report, at http:/ec.europa.eu/transport/air_portal/international/pillars/global_partners/doc/us/final_report_bah.pdf

Europeans carriers cannot fly passengers from LA to NY. Wilmington should not be used as a pawn in global aeropolitics and a "cargo first" policy should not be pursued.

Along the same lines, I would draw this Committee's attention to the upcoming U.S.-EU Air Transport negotiations, the next meeting of which is later this month. John Byerly, Deputy Assistant Secretary for Transportation Affairs and Chief Negotiator for the U.S. has stated that "sweeping away" nationality requirements is a goal of Stage Two negotiations.[14] For the reasons I've already stated, this Committee should do everything within its power to prevent the inclusion of such a provision in any agreement resulting from Stage Two U.S.-EU Air Transport negotiations.

Give Wilmington a chance

UPS and DHL collusively assert this is just politics. But the restructuring proposed by Deutsche Post, if allowed, will be a real economic disaster for Wilmington, Ohio. More than 8,200 jobs will be unnecessarily destroyed in a small town of about 13,000 people. Many of the maintenance workers and sorters have worked at the DHL Air Park, formerly the Airborne Air Park, for decades. Many work through the night while living on their family farms in rural Ohio. Their jobs provide health insurance that has allowed them to work those farms in addition to earning a paycheck. The tax base will be devastated, medical and school funding will suffer, and small businesses will suffer. The psychological impact on families, with layoffs of this scale, will be long-term. For wage earners who support their families, there will be trauma when they are no longer able to provide for their children. For many, this will be the most traumatic event in their lives.

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[14] John R. Byerly, Remarks to the European Aviation Club, Brussels, Belgium, May 13, 2008. http://www.state.gov/e/eeb/rls/rm/2008/104651.htm.

DHL says they have a cost problem, but not once have they approached me for labor concessions, directly or indirectly. As a labor leader, I am honored to represent the hard-working and professional pilots of ABX Air and the community of Wilmington, Ohio. These are Ohioans. These are Americans. Even after DHL's devastating announcement, they continue to provide impeccable performance. They show up every day, holding onto hope that DHL will change its mind. They hope that their willingness to work hard will be recognized, and that DHL will do the right thing. They work hard. They keep performing. They don't want meager hand-outs and false promises, they want jobs. They are loyal and committed employees that can perform just as well, if not better, than anybody else in this business. Give them a chance.

Mr. Chairman, you and this Committee can help give them that chance.

We respectfully request you oppose the deal between DHL and UPS as an affront to U.S. aviation policy, which seeks to promote competition in the air transportation industry and discourage excessive market domination. We ask that you request that this Justice Department initiate an investigation and enforce the antitrust laws of this country in defense of America's aviation industry, and resist any attempts to grant DHL a waiver of the foreign ownership restrictions that keep our country safe and ensure the fair application of our labor laws.