

STATEMENT

OF

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

BEFORE THE

JUDICIARY COMMITTEE
U.S. HOUSE OF REPRESENTATIVES

ENTITLED

"COMPETITION IN THE PACKAGE DELIVERY INDUSTRY"

PRESENTED ON

SEPTEMBER 9, 2008

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Mr. Chairman 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. 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 raised 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 anti-competitive effects of this deal. We are grateful this issue has raised such an important and necessary policy discussion as it impacts the workers I am honored to represent. Mr. Chairman, I respectfully request that this Committee demand that this Justice Department initiate an investigation and enforce the antitrust laws of this country.

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 on the elimination of competition in the domestic air express market brought about by a proposed transaction between two dominant air express carriers - DHL and UPS. 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 backing 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.

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 Country 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 praised the complimentary service portfolios of the two airlines and Airborne's broad ground network.

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 attended by the Mayor of Wilmington, Ohio. That was two days before DHL's announcement that will devastate Wilmington, Ohio.

DHL's entry into the U.S. market triggered a proceeding before the Department of Transportation because of well-established citizenship laws for U.S. air carriers, and the airlines that carry 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 southwest at the Cincinnati/Kentucky International Airport. DHL effectively controlled these two express cargo airlines 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 (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 in cities like Roanoke, Virginia.

Through the 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 of express delivery service.

In the air express business, on-time-performance is critical to customer service. 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 and 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 collapse 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 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 with 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.

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 aircraft are equipped to handle packages in "C" containers rather than "A" containers. 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 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 a 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?

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 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.¹

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 transit, to sort, to transit, and 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, 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

¹ “FedEx Eyeing Deal to Buy DHL”, Ken MacFadyen, Mergers & Acquisitions Report, Feb. 4, 2008.

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. Consistent customer service and real pricing pressure will come only from true competition.

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. It makes no sense to announce a deal like this before the terms of the deal are 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%. 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 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.

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 earliest DHL can deliver “DHL Next Day” service is one week. The earliest

DHL can deliver an express package from D.C. to a district office in Lorain, Ohio is noon. The earliest they can deliver an express package from D.C. to La Crosse or Ladysmith, Wisconsin is 5 pm, but still listed as “DHL Next Day 12 pm”. The earliest they can deliver from D.C. to Harrisonburg or Staunton, Virginia is 5 pm. For Big Stone Gap or Pulaski, Virginia, as well, the earliest they deliver is 5 pm. 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 with 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.

A justification given by this profitable global corporation for their restructuring decision is the foreign ownership restrictions in the U.S. The citizenship rules for U.S. airlines are well-established. As became apparent in 2001, after fanatics decided to use airplanes as their weapon of choice, the airline business is different than other businesses. Our citizenship laws ensure close oversight of U.S. air carriers to ensure the highest level of safety and security for the traveling public and the people living below America’s airspace. The airline industry has unique labor concerns because of the mobile labor dynamic involved, and the citizenship laws allow our labor laws to be properly applied. Finally, our citizenship laws ensure our passenger and cargo airlines are fully available to the Civil Reserve Air Fleet (CRAF) to fulfill the unique interrelationship between civil

and military use. Furthermore, it is doubtful Deutsche Post and DHL Express would have done anything differently if they had a 51.1% or greater ownership interest in Astar rather than the 49% ownership interest they have.

The restructuring proposed by Deutsche Post, if allowed, will be an 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.

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 ask the Antitrust Division of the Justice Department to review this transaction. And Mr. Mullen, if you are so confident of your position, why don't you voluntarily submit to a Department of Justice review and silence your critics.