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News Release

Letter to the Hon. Martin Cauchon

Letter to the Hon. Alfonso Gagliano

Revenue Chart

Canadian Taxpayers Federation
Federal Office, Suite 512-130 Albert Street,
Ottawa, ON   K1P 5G4
Phone: 613-234-6554
Fax: 613-234-7748

Web: www.taxpayer.com

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Canada Post Overview

Canada Post Corporation (CPC) is a Crown Corporation of the Government of Canada. CPC's activities range from the delivery of first-class lettermail (a monopoly which is conferred on Canada Post through statute) to full competition with the private sector in the areas of courier services, electronic mail services and international consulting operations.

According to its 1999-2000 Annual Report, CPC is Canada's 5th largest employer with 65,000 full and part-time employees and consolidated annual revenues of $5.637 billion.

Recent Milestones

October 16, 1981	With passage of the *Canada Post Corporation Act*, the former Post Office department becomes the Canada Post Corporation, a Schedule One Crown Corporation of the Government of Canada.
June 4, 1993	Canada Post (CPC) enters into negotiations and agreement with ONEX Corporation to purchase 75% of Purolator Courier.
September, 1993	Canada Post introduces XPRESSPOST for customers looking for a cost-effective alternative to courier and regular mail for sending time-sensitive documents.
November, 1993	CPC completes its acquisition of 75% of Purolator Courier for $55 million plus an assumption of debt.
January, 1994	Canada Post joins five key players in a consortium called UBI which merges the Corporation on the electronic highway. Partners in UBI are Hydro-Québec, the National Bank of Canada, Loto-Québec, Vidéoway Communications Inc., the Hearst Corporation and Le Group Vidéotron Ltée. Through their home television equipped with a two-way terminal connected to local cable service, users of this service will be able to bank, shop or send electronic mail from their home.
March 27, 1994	Canada Post Corporation becomes subject to corporate income tax pursuant to Regulation 7100 of the *Income Tax Act* that adds CPC to the taxable list of federal Crown Corporations.

January, 1995	Launch of SkyPak, CPC's new international courier service.
November, 1995	The Minister responsible for Canada Post Corporation launches the Canada Post Mandate Review. The purpose of the Mandate Review is to: 1) review the functions that CPC currently carries out and those which should be provided in the future, 2) conduct an analysis of CPC's business lines in light of the heightened competition being experienced in many product and service areas; and 3) assess the ability of CPC to adjust to market conditions and determine whether such adjustments are appropriate.
February, 1996	Canada Post Corporation and IBM Canada Ltd. sign a letter of intent enabling the two companies to jointly evaluate, develop and address various opportunities in electronic commerce.
July 31, 1996	The Hon. Diane Marleau, Minister responsible for Canada Post Corporation, releases the report of the Canada Post Mandate Review. The Review, headed by George Radwanski, is very critical of Canada Post's non-core activities, including courier operations.
March, 1997	Canada Post paid a dividend of $10 million to the people of Canada through the federal government. The payment was based on the net income that the Corporation realized during the 1995/96 fiscal year.
January 6, 1999	Acquisition of the remaining 22.9% of Purolator shares from ONEX Corporation was concluded for $66 million.
July, 2000	Purolator International courier service is launched.
July, 2000	XPRESSPOST service is extended to the U.S.A.

The Tax-Loss Carry Forward

For the year ending March 26, 1994, Canada Post Corporation (CPC) recorded a net income loss of $270,390,000 in its Annual Report. Note #10 which forms part of CPC's Annual Report for the following year (1994/1995), states that:

> On March 27, 1994, Canada Post Corporation became a prescribed Crown Corporation for tax purposes and as such is subject to federal income taxation under Part 1 of the Income Tax Act.

The same Note goes on to state that "consolidated tax loss carry-forwards in the amount of $320,000,000 are available to reduce future income taxes and will expire by the year 2002. The benefit of these tax-loss carry forwards and net unclaimed tax deductions have not been recognized in the Corporations' consolidated financial statements."

From the previous year's Annual Report (1993/1994), Note #5 stipulates that $46,000,000 of tax loss carry forwards and $8,000,000 in net unclaimed tax deductions accrued to Canada Post due to the acquisition of Purolator Courier.

However, it appears that the $270,390,000 net loss for the same period was booked as a tax-loss carry forward for future years.

The Problem:

Since Canada Post was exempt from federal income taxation prior to March 27, 1994, how can it "claim" and carry forward a tax loss when it wasn't subject to pay federal income taxes in the first place?

The CTF analysis *(see attached spreadsheet)* follows this tax-loss carry forward through the past seven Annual Reports. It appears as though CPC was granted a "sweetheart tax deal" giving the corporation a $270 million tax free holiday to better leverage its competitive position in markets where it does not enjoy legislative monopoly protection (ie: courier services).

Furthermore, this tax free holiday runs counter to a Regulatory Impact Assessment Statement released by the Government on June 2, 1994 which noted that "Canada Post operates on a commercial basis with other service providers for a significant share of its revenues. Making Canada Post taxable will place the corporation on a more even footing with its private-sector competitors."

Question for the Minister Responsible for the Canada Customs and Revenue Agency:
Is this tax-loss carry forward legal?

A "Nationalized" Courier Company

As seen in the section entitled ***Recent Milestones***, Canada Post has acquired almost 100% total ownership of Purolator Courier in share purchase transactions from ONEX Corporation dating back to November 1993.

Purolator Courier is Canada's largest full-service courier company with an estimated 47% of the Canadian courier market. This large market share conveys as position of market dominance. Purolator's performance for 1999, according to CEO Fred Manske, was "disappointing. Revenue was below what we projected, and our expenses were only slightly better than the business plan. The end result was a net loss of $2.3 million for the year."

A recent independent analysis of Purolator's performance conducted by the chartered accounting firm BDO Dunwoody on behalf of the Canadian Courier Association and obtained by the Canadian Taxpayers Federation paints a dismal picture of Canada Post's investment in Purolator Courier.

The report's three main conclusions are as follows:

- In comparing the results of CPC's purchase of the shares of Purolator, the results achieved to date are discouraging. Canada's lettermail service would probably have been better served by less risky investments such as Government of Canada Bonds.

- Insofar as Purolator's performance has lagged behind that of the industry, CPC's investment has not been successful.

- Based on the foregoing, the objectives of the Government of Canada and CPC … have not been met.

In addition, George Radwanski, Chairman of the Canada Post Mandate Review cautioned the Government of Canada about Canada Post's involvement with Purolator throughout his report dated July 31, 1996. Consider the following passages from the Radwanski report:

- The Corporation has created serious issues of fairness and appropriateness by "leveraging" the network it has built up through its government-granted lettermail monopoly and through past outlays of public funds to compete with private sector companies from a position of strength they cannot match. (page 2)

- … it is difficult to see Canada Post's major sally into the courier industry through the 1993 acquisition of Purolator Courier is anything other than remarkable. The corporation in effect nationalized Canada's largest private sector courier company. (page 36)

- As a general principle, Canada Post should no longer engage in competition with the private sector in areas outside its core postal services mandate … With regard to exiting from the courier business, some precision of definition is appropriate. Clearly, Canada Post should divest itself from Purolator. (page 84)

Above and beyond the clear direction advocated by Mr. Radwanski (which four years after the fact remains ignored), divestiture of Purolator Courier would be consistent with government policy as articulated by the Hon. Paul Martin, Minister of Finance, on page 14 of his 1995 Budget Speech. Mr. Martin noted that:

> *The government is committed to privatizing and commercializing government operations wherever that is feasible and appropriate. This is a matter of common sense. Our view is straightforward. If government doesn't* **need** *to run something, it* **shouldn't**. *And in the future, it* **wont'**.

Finally, associations from the Canadian Courier Association to the Canadian Industrial Transportation League have also repeatedly urged the government to "get out" of the courier business by justifiably arguing that the Canadian economy is well-served by a mature and highly competitive private courier industry.

Question for the Minister Responsible for Canada Post:
Given the dismal return Canada Post Corporation (and in return Canadian taxpayers) has generated from its investment in Purolator Courier and the "conflict of interest" with stated Government policy which CPC's ownership of Purolator continues to represent, isn't it time that Canada Post wholly divest its ownership of Purolator entirely through an outright and true privatization of Purolator Courier?

Is Canada Post Abusing its Monopoly Position?

Section 14.1 of the *Canada Post Corporation Act* gives Canada Post exclusive license and domain to deliver first-class lettermail within Canada. The act grants that "the Corporation has the sold and exclusive privilege of collecting, transmitting and delivering letters to the addressee thereof within Canada."

To be fair, Canada Post has built an extensive infrastructure to carry though on this "service mandate" to Canadians. According to the Canada Post web site:

- The Corporation's delivery network expands by approximately 170,000 addresses every year;
- Canada Post offers customers a network of 18,600 retail points of access.
- There are 15,600 letter carrier routes in Canada;
- There are over 750 planned domestic flights carrying mail every business day;
- There are over 200 planned flights entering and leaving Canada carrying mail every business day;
- Canada Post's fleet of vehicles is among the largest in Canada with over 6,000 vehicles, logging more than 74 million kilometres during the year; and
- Including street letter box sites, community mail box sites, retail outlets, rural lot-line boxes, etc., there are 936,000 possible points of entry to Canada's postal system.

While this infrastructure is impressive, it is also being used to cross-subsidize Canada Post's non-core operations which compete with the private sector.

Indeed, this cross subsidization was a key issue which figured in the Radwanski Mandate Review report. The report noted that:

- Canada Post's competitors complain that the corporation is able to use its network to leverage cost savings for its competitive products. They point to such activities as piggybacking lettermail onto Purolator flights, piggybacking courier products onto mail trucks, and combining services in the provision of volume electronic mail, media cards and the operation of business centres. (page 46)

- Canada Post openly admits that **it does** and **will continue** to leverage its existing network to achieve cost savings in the provision of all its product lines. It argues that this is merely efficient use of resources and sound business practice. The difficulty is that, for instance, by using the same airline as Purolator for its lettermail shipments, Canada Post is causing the overall costs per piece of transporting both products to decline through volume discounts. (page 46)

- The leveraging issue underscores the fundamental problem with Canada Post's competitive activity. It is undoubtedly true that other multi-product companies regularly use leveraging of their networks to maximize efficiency – but these private sector companies did not build their networks with public funds, on the foundation of a government-granted monopoly. None of Canada Post's competitors have access to the cost advantages that such a network automatically provides. (page 47)

This cross-subsidization issue has also become the focus of a $230 million NAFTA lawsuit filed by courier giant United Parcel Service of America, Inc. (UPS). The lawsuit represents a Statement of Claim against the Government of Canada (read: Canadian taxpayers) in which UPS alleges, amongst a variety of allegations, that Canada Post cross-subsidizes it's courier operations by giving it's non-monopoly courier products access to the distribution system set-up in order to deliver first-class lettermail.

Moreover, in the last 30 days, <u>two other examples</u> of blatant cross-subsidization have occurred.

On July 1st, Canada Post retail outlets began to sell Purolator Courier products. This is clearly an example of using the retail presence designed to serve the first-class letter mail monopoly to cross-subsidize CPC's subsidiary, Purolator Courier. This ability to sell courier services is not available to other courier companies such as UPS, CanPar, Loomis, or Greyhound right down to regional and metropolitan based courier companies.

The Problem: This business expansion exercise blurs the line between Purolator and Canada Post and is a blatant example of cross-subsidization.

On July 8, 2000, Canada Post delivered up to 100,000 first print-run copies of the much anticipate children's novel *Harry Potter and the Goblet of Fire.* This special "Saturday delivery" was conducted for Chapters Online. The business strategy behind this special delivery seems sound enough: Chapters Online was mirroring the activities of American competitor Amazon.com which inked a deal with FedEx for overnight delivery of the book in the continental U.S. The problem lies in the fact that, according to the June 29th edition of the *National Post*, Canada Post enlisted "the men and women who normally empty mailboxes on Saturdays to deliver the much sought after books for Chapters Online."

The Problem: Again, the men and women who empty mailboxes are employed to empty first-class lettermail and their salaries are derived from Canada Post's first-class lettermail monopoly protection. This is another blatant example of Canada Post's abuse of its monopoly power.

Canada Post is now also actively involved in the fields of banking and electronic commerce not to mention its international consulting and implementation activities.

Question for the Minister Responsible for Canada Post:
Why is Canada Post allowed to continue to abuse its monopoly position and in the process jeopardizing Canadian taxpayers through the threat and real potential for further NAFTA lawsuits or domestic challenges through complaints filed with the federal competition tribunal ?

Next Steps for the Government

The CTF has posed the questions outlined in this document to the appropriate Ministers of the Crown and advised the Prime Minister of Canada as to the seriousness of the issues raised with respect to Canada Post's operations and tax-loss carry forward status.

In the interim, the CTF recommends the following:

1) Canada Post should immediately seek to divest all holdings of Purolator Courier in the most realistic time frame possible. If necessary, legislation should be drafted and tabled in the House of Commons (either separate legislation or amendments to the *Canada Post Corporation Act*) this fall to expedite this process.

2) The Minister responsible for Canada Post must immediately establish and independent review of all non-core activities currently conducted by Canada Post. This review must catalogue all activities in which Canada Post is competing with the private sector and then seek to divest itself from these operations consistent with the privatization and commercialization policy framework laid out in the 1995 Federal Budget.

3) That the Prime Minister coordinate the activities of the relevant Ministers in response to the concerns raised herein and report back to Canadians as soon as possible on other corrective measures which will ensure that Canada Post can fulfill its mandate while simultaneously protecting the Government of Canada and ultimately, Canadian taxpayers, from future financial liability as a result of international or domestic legal actions.