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# Crisis in the Mail: Fixing a Broken International Package System

*Arthur Herman*

*February 2017  
Commission  
Report*





Hudson Institute

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Fixing a Broken  
International  
Package System**

**Arthur Herman**



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## ***Executive Summary***

**I**nternational shipping of packages has become an important cog in the global economy, fueled by a growth in e-commerce averaging 19 percent a year since 2000. E-commerce makes it possible for Americans to order goods from China, Hong Kong, Singapore, India, and other countries literally with the click of a button.

The Universal Postal Union (UPU) is the United Nations agency that regulates the government-to-government overseas postal package system. The primary international agreement of the UPU governing the international postal system is the “Universal Postal Convention” (or, informally, the “UPU Convention”), to which the U.S. Department of State traditionally acts as negotiator and signatory.

Unfortunately, the Hudson Postal Commission has found that the current Convention:

- 1) Disadvantages U.S. merchants in their competition with foreign merchants;
- 2) Imposes net costs on the United States Postal Service of tens of millions of dollars each year, which translates into costs for U.S. consumers;
- 3) Presents serious security risks in terms of combatting terrorism and other threats;
- 4) Facilitates importation of illegal pharmaceuticals and illicit drug shipments; and
- 5) Costs the U.S. government millions of dollars in lost customs revenue.

As this report details, a tangle of outdated and anti-competitive international rules promulgated by the UPU make having a strong, safe, and secure post system increasingly difficult, particularly when it comes to handling small packages (weighing less than 2 kg, or 4.4 lbs) arriving from overseas.

After studying the available data and evidence, and after hearing testimony from multiple witnesses, the members of the Hudson Postal Commission have agreed to make the following policy recommendations:

- Limit the Department of State to the negotiation of international postal agreements which implement broad, commercially neutral governmental policies and are consistent with U.S. policies towards trade in services generally.
- Clarify the application of antitrust policy and trade law to international postal services.
- Appoint a high-level commission to review U.S. participation in the UPU and make recommendations for steps needed to advance the national interest.
- Create an inter-agency task force to negotiate an agreement among industrialized countries establishing non-discriminatory principles for terminal dues and other charges for the delivery of inbound international mail with a target date of January 1, 2018.

- Initiate a study at the World Customs Organization of harmonized rules for customs and security controls that could be applied to all low-value packages.
- Increase the U.S. Postal Regulatory Commission's oversight of the Postal Service, especially with regard to the collection of data for, and the handling of, inbound international packages.
- Apply U.S. customs and security laws and regulations in the same manner to postal shipments and non-postal shipments while allowing a reasonable transition period for foreign Posts in developing countries.

Having a strong, but also safe and secure, United States Postal Service that can handle more than 474 million pieces of foreign mail every year should be an important national priority. The Hudson Commission believes these important steps will help to achieve that goal, and to make sure that our international agreements regarding delivery of overseas mail are consistent with U.S. trade, antitrust, national security policy and law.

## **Introduction**

**I**nternational shipping of packages has become an important cog in the global economy, fueled by a growth in e-commerce averaging 19 percent a year since 2000.<sup>1</sup> E-commerce has allowed American online shoppers to make direct purchases from around the world, which are then shipped to the United States and delivered by either the United States Postal Service or private carriers like FedEx and UPS.

E-commerce makes it possible for Americans to order goods from China, Hong Kong, Singapore, India, and other countries literally with the click of a button. That means hundreds of thousands of packages arrive in the U.S. each day from those same countries via the international postal system, with no check on whether they contain illegal or even dangerous materials.

Very few customers give much thought to whether a clock radio or battery charger or bottle of shampoo is delivered by the Postal Service, on the one hand, or by private carriers, on the other. But strangely, the rules governing how the shippers handle that package in terms of cost, customs, and security protocols, differ widely.

Indeed, there is an alarming disparity between how packages are handled by private carriers and how they are handled by national Posts, including the Postal Service — a disparity that reflects an outdated international postal services agreement *and* the system of subsidized international package shipping it fosters.

The Universal Postal Union (UPU) is the United Nations agency that regulates the government-to-government overseas postal package system. The primary international agreement of the UPU governing the international postal system is the “Universal Postal Convention” (or, informally, the “UPU Convention”). Unfortunately, as this report will indicate, the current Convention:

- 1) Disadvantages U.S. merchants in their competition with foreign merchants;
- 2) Imposes net costs on the Postal Service of tens of millions of dollars each year;
- 3) Presents serious security risks in terms of combatting terrorism and other threats;
- 4) Facilitates importation of illegal pharmaceuticals and illicit drug shipments; and
- 5) Costs the U.S. government millions of dollars in lost customs revenue.

According to the Postal Regulatory Commission (PRC), 474 million pieces of foreign “letter post” mail (i.e., documents and packages weighing less than 2 kg, or 4.4 lbs)

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<sup>1</sup> Lavigne, Grace M. "E-commerce Growth Reshapes Traditional Supply Chains." *The Journal of Commerce*. 13 Oct. 2014. Web.

entered the U.S. in 2015, of which the UPU estimates one-fifth consists of small packages. That implies that something on the order of 100 million packages entered the U.S. with no accountability in terms of electronic data information, or accountability regarding the overall cost of overseas postal shipments to our own U.S. Postal Service.<sup>2</sup>

U.S. participation in the UPU is governed by the Postal Accountability and Enhancement Act of 2006 (PAEA), the first major revision of the nation's postal laws since 1970.<sup>3</sup> Among other reforms, the PAEA comprehensively revised the international postal policy of the United States and the role of the PRC in reviewing international postal services. The PAEA committed the U.S. to promote and encourage international postal agreements that foster "efficient operation of international postal services and other international delivery services" and "unrestricted and undistorted competition in the provision of international postal services and other international delivery services" (except for services covered by the U.S. postal monopoly). The PAEA thus shifted the focus of U.S. policy from promoting the operations of international postal services *per se* to supporting the emergence of an efficient and competitive system of public and private delivery services.<sup>4</sup>

Under the PAEA, the Secretary of State is responsible for the negotiation and conclusion of international postal agreements at the UPU. The Secretary's authority is limited, however. The Secretary may not conclude any convention which would grant an "undue or unreasonable preference" to the Postal Service, a private carrier, or any other person in the provision of competitive postal services. Nor may the Secretary negotiate an agreement relating to non-monopoly postal services that is contrary to U.S. antitrust laws or that would prevent federal agencies from applying customs and other import and export laws "in the same manner" to competitive products offered by the Postal

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<sup>2</sup> Postal Regulatory Commission, *Financial Analysis of United States Postal Service Financial Results and 10-K Statement: Fiscal Year 2015* (Mar. 29, 2016), page 88, reports that the volume of "Inbound Single-Piece Mail Intl" in 2015 was 473.7 million items. This category includes inbound "letter post" packages called "small packets" which weigh up to 2 kg (4.4 lbs). The Commission has declined to make public what percentage of these items are small packets, but a study by the Universal Postal Union estimated that 20.9 percent of the letter post items received by industrial countries in 2014 were small packets. Since the percentage of small packets in the letter post is increasing each year, it appears that volume of small packets received by the Postal Service in 2015 was on the order of 99 million items, or about 270,000 per day. In addition, the Postal Service received additional inbound packages in the "parcel post" and "EMS" (express mail) packages (also undisclosed by the Commission), although the volume of packages received via these services is likely much smaller than the volume of small packets.

<sup>3</sup> Postal Accountability and Enhancement Act of 2006. Pub. L. 109-435. 120 Stat. 35. 20 Dec. 2006. Washington: GPO, 2001. The Library of Congress. PDF file. The provisions establishing the PRC are found at 39 U.S.C. §§ 501-505. The Postal Regulatory Commission replaced the Postal Rate Commission, a regulatory agency created in 1970 with a more limited mission.

<sup>4</sup> 39 U.S.C. § 407(a).

Service and U.S. private carriers.<sup>5</sup> In addition, the Secretary is directed to coordinate the development of the U.S. position at the UPU with other federal agencies, including the Postal Regulatory Commission, the Department of Commerce, the Department of Transportation, and the Office of the U.S. Trade Representative.

Having a strong, but also safe and secure, United States Postal Service is an important national priority. It is the lynchpin of a \$1.4 trillion mailing industry that employs some 7.5 million Americans.<sup>6</sup> Unfortunately, as we shall see, a tangle of outdated and anti-competitive international rules promulgated by the UPU make having a strong, safe, and secure post system increasingly difficult, particularly when it comes to packages arriving from overseas.

The Hudson Postal Commission (“Commission”) met in Washington, DC on September 10 and 11, 2016. This final report draws from the most recent data concerning the manifold problems of the international government parcel post system, in order to provide an overview of the growing crisis in international package delivery.

The second part of this report presents a series of concrete policy recommendations for fixing and reforming the system, with a focus on a multi-dimensional, multi-agency approach — including concrete steps Congress needs to take to make sure our Postal Service is safe and secure.

Any discussion of these issues, however, must begin with the nature and structure of the Universal Postal Union.

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<sup>5</sup> 39 U.S.C. §§ 407(b)(1), 407(b)(2)(A), 407(e)(2), 409(e).

<sup>6</sup> "Size and Scope - Postal Facts." *United States Postal Service*. 13 Jan. 2016. Web.

### **What is the Universal Postal Union (UPU)?**

Originally created in 1874 and since 1948 a specialized agency of the United Nations,<sup>7</sup> the Universal Postal Union (UPU) was established to create “a single postal territory for the reciprocal exchange of correspondence” between the Union’s twenty-one leading countries.<sup>8</sup> The international postal system was extended to the conveyance of packages by stages. It was in 1929 that “small packets” were added to the international postal convention.<sup>9</sup>

The UPU establishes rates and standards for the postal delivery of documents and packages exchanged among its member countries, which have now grown to 192 in number.<sup>10</sup> Unfortunately, in recent years the UPU has become an obstacle to, rather than a facilitator of, making the international package shipping system more efficient, more modernized and standardized, and safer. It has also begun to impose unsustainable costs on the Postal Service.

Member countries within the UPU agree that their Posts will carry one another’s documents and packages from their point of arrival, for example a port or airport, to their final destinations. Each Post in turn is obliged to compensate the others for this inbound delivery service with fees set by the UPU.

The fees applicable to the delivery of “letter post” mail — documents and most packages weighing up to 2 kg (i.e., 4.4 lbs) — are known as “terminal dues.”<sup>11</sup> They are set every four years in a new version of the Universal Postal Convention adopted by a general “congress” of the UPU. The current Universal Postal Convention was adopted by a UPU Congress held in Doha in 2012. It is in effect from January 1, 2014, to December 31, 2017. The most recent UPU Congress took place in Istanbul in September and October 2016. It adopted a new Universal Postal Convention that will be in effect during the period 2018 to 2021. The terminal dues established in the Universal Postal Convention are the legal default rate for delivery of inbound documents and small packages. Posts can agree on alternative rates in a bilateral or multilateral agreement, but alternative arrangements are usually closely related to UPU terminal dues rates.

How the current UPU Convention determines terminal dues is based on a complex classification of individual countries according to their level of economic and postal development. In 2012, the Doha Congress organized its member countries into six

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<sup>7</sup> "The UPU." *Universal Postal Union*. Web.

<sup>8</sup> General Postal Union, art. 1, 19 Stat. 577, (1874). Copies of UPU conventions from 1874 through 1949 may be obtained from the Library of Congress at <https://www.loc.gov/law/help/us-treaties/>.

<sup>9</sup> Universal Postal Convention 1929, art. 32, 46 Stat. 2523, 2540 (1929).

<sup>10</sup> "The UPU." *Universal Postal Union*. Web.

<sup>11</sup> Universal Postal Convention 2012, arts. 29-31. Rates for delivery of “parcel post” items — packages up to 20 kg (44 lbs) — are called “inward land rates” and established by a UPU committee of 40 postal officials called the Postal Operations Council, *Ibid.*, arts. 34-35.

groups, for the purpose of defining terminal dues and other charges.<sup>12</sup> In general, the higher the group number of a country, the less the Post charges for the delivery of inbound international packages and the less it pays for the delivery of packages sent to countries in the categories with lower numbers.

- Group 1.1 includes the United States, Japan, Australia, and most of the world's other developed economies, as well as most of the overseas territories belonging to Great Britain and France.
- Groups 1.2 and 2 apply the same terminal dues schedule for inbound and outbound letter post. Group 1.2 includes more recently advanced countries, such as Hong Kong and Singapore. Group 2 consists of countries with mid-size economies such as Cyprus, Hungary, Estonia, Poland, Slovakia, and Saudi Arabia.
- Group 3 includes still emerging economies such as Argentina, Bosnia, Brazil, Chile, Jamaica, Gabon, Cuba, Kazakhstan, as well as the People's Republic of China.
- Groups 4 and 5 apply the same terminal dues schedule for inbound and outbound letter post. These groups generally include least developed countries, but they also include countries with substantial economic potential such as Egypt, India, Iran, Kenya, Nigeria, and Vietnam.

The appearance of China, the world's second-largest economy, in the Category 3 grouping highlights a fundamental flaw in the UPU ranking system for terminal dues. That ranking is defined by a "postal development index" based on the level of postal service within that country.<sup>13</sup> This overlooks the fact that a country such as China may have a relatively low level of domestic postal development for historical reasons — in China's case, its modernization came after the era of paper-based communications — but may actually be a major player in international commerce, particularly e-commerce.

In other words, what a business should be paying for delivery of its e-commerce shipments in a foreign country has nothing to do with the state of development of its national postal service. Yet the current UPU ranking system inappropriately links the two.

Illogical categorization has significant consequences both for the integrity of the UPU, as well as for those Posts like the Postal Service (and their customers) who shoulder the major burden of subsidizing the world's global postal system and for those Posts like China Post that benefit from it (see Section 4).

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<sup>12</sup> Universal Postal Union. *Classification of countries and territories for terminal dues and Quality of Service Fund (QSF) purposes*. Lists of Resolution C 77.2012, as amended by the 2013 CA decisions. PDF file.

[http://www.upu.int/uploads/tx\\_sbdownloader/listCountryClassificationEn.pdf](http://www.upu.int/uploads/tx_sbdownloader/listCountryClassificationEn.pdf)

<sup>13</sup> *Decisions of the 2012 Doha Congress*. Proc. of Universal Postal Union Convention, Qatar, Doha. Berne: International Bureau of the Universal Postal Union, 2013. 132. Universal Postal Union. PDF file.

So while the domestic postal systems in the United States, the European Union, and other advanced countries have become steadily more liberalized and focused on encouraging competition from the private sector as well as introducing new technologies to make the postal systems more efficient and more accountable, the UPU has moved in the opposite direction. It has evolved into an international cartel of government-sponsored Posts, who use its rules to protect low postal rates for some, including low package rates, while forcing domestic mailers and a handful of advanced countries to underwrite the costs of the system.

At the same time, the international postal system that the UPU oversees has also evolved. Until the last quarter of the twentieth century, the primary purpose of the UPU was to coordinate the exchange of documents between governmental postal administrations, each of which had a monopoly on the carriage of letters. Today, in most industrialized countries and many developing countries, the “Posts” are no longer government administrations but corporatized, and often privatized, successor companies that engage in multiple lines of business. Their primary aim is profits, not public service.<sup>14</sup> The purpose of the UPU has shifted to advancing the commercial interests of these successor Posts in an international market increasingly dominated by conveyance of packages, particularly packages generated by the explosive rise of e-commerce since 1999.

In short, postal operators are increasingly turning into package services as a way to grow their international business. For example, e-commerce small packets (less than 2 kg) from China to the United States increased 182 percent from 2011 to 2012, from 9.5 million packages to 26.8 million — almost a *three-fold increase*.<sup>15</sup>

According to the UPU’s own studies, between 2010 and 2014 packages increased from about 12 percent to nearly 25 percent, or one-quarter, of international mail volume and more than half the weight.<sup>16</sup> Indeed, by the time the rules established by the 2016 Istanbul Congress expire in December 2021, packages will likely constitute the majority of international postal shipments.

As a representative of one of the private carriers explained to the Commission, “What was once an institution that provides a means of linking the world together for societal reasons has morphed into an intergovernmental organization whose real mission has become the promotion of the commercial success of the world’s post offices.”

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<sup>14</sup> See Accenture Consulting, “Achieving High Performance in the Post and Parcel Industry: Accenture Research and Insights 2015” (2016). PDF file. <https://www.accenture.com/us-en/insight-achieving-high-performance-post-and-parcel-industry>.

<sup>15</sup> U.S. Postal Service, Office of the Inspector General, “Inbound China ePacket Costing Methodology: Audit Report” (Feb. 25, 2014), p. 3.

<sup>16</sup> UPU, POC C 3 LPRG 2014.2 Doc 4a, Annex 1, table 9 (Results of the items per kilogramme (IPK) study) (Oct. 10, 2014).

Today, leading postal operators see international e-commerce shipments primarily as a business opportunity and revenue generator. From 2012 to 2016, for example, Singapore Post's international mail revenue soared by 85 percent, almost all of it fed by e-commerce: an astonishing example of how a government-sponsored postal company (Singapore Post is 74 percent privately owned, with Chinese online mega-retailer Alibaba owning 10 percent<sup>17</sup>) can profit from an international postal system that's geared to benefit some countries, while penalizing others.<sup>18</sup>

"Penalizing" is not an exaggeration. The sobering fact is that a Post in a developed country which has high costs in wages, services, and infrastructure, generally loses money on every piece of international mail that arrives on its shores or crosses its border. For example, Norway Post, which has publicly stated that the money it loses under the UPU system has to be made up by charging more to Norwegian customers, is one of those Category 1.1 nations that are in effect subsidizing other countries' postal services.<sup>19</sup>

Another country being penalized is the United States. To understand why and how, it is important to realize that the massive surge in e-commerce, particularly coming from Asia, has come at considerable cost both to U.S. businesses and the Postal Service, thanks mainly to the UPU terminal dues system.

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<sup>17</sup> Singapore Post, *Transforming for the Future: Annual Report 2015/16* (2016), p. 218. Alibaba has agreed to purchase an additional 5 percent of Singapore Post. Forbes, "Alibaba Steps Up Asia Logistics Presence With New SingPost Investment" (Jul. 7, 2015). <http://www.forbes.com/sites/ywang/2015/07/07/alibaba-steps-up-asia-logistics-presence-with-new-singpost-investment/#60ed165d290a>.

<sup>18</sup> Singapore Post, "Q4 & Full Year [Fiscal Year] Results Financial year ended 31 March [Year]" (annual). <http://www.singpost.com/about-us/investor-centre/financial-results>.

<sup>19</sup> Morris, David Z. "The United Nations Is Helping Subsidize Chinese Shipping. Here's How." *Fortune*. 10 Mar. 2015. Web.

## **How the UPU Disadvantages U.S. Merchants in Their Competition with Foreign E-Commerce**

**E**-commerce is not only becoming the dominant source of international post shipping, it's also become a driving engine of the world's developed economies. This is particularly true for China.

China has been a manufacturing powerhouse for several decades, but the country's leadership now sees e-commerce as a way to sustain economic growth by spurring consumption at the same time that it revives exports.<sup>20</sup>

Although China's overall trade volume fell by 7 percent in 2015, the first decline since 2010, and exports fell by 13.2 percent,<sup>21</sup> e-commerce exports increased by 30 percent.<sup>22</sup> In addition, China is home to the world's single largest e-commerce market, with e-commerce expected to supply 42 percent of domestic consumption growth, even as the numbers of Chinese e-commerce businesses now number in the scores.<sup>23</sup>

In 2013 Chinese online sales reached \$314 billion, or 35 percent of all world e-commerce sales (by comparison, U.S. online sales were \$255 billion). An increasing percentage of those sales are export sales to other countries like the U.S.<sup>24</sup> — and UPU rules are providing an additional boost for those sales.

How so? It is important to remember that the UPU sets rates for delivery of postal items sent from country to country, i.e. what's charged back and forth, based on their state of economic and domestic postal development. Category 3 countries like Gabon, for example, get a price break (compared to domestic postage) on the packages it ships to Norway, that Norway doesn't get shipping to Gabon — or to the United States, another Category 1.1 country.

Since China, the world's second-biggest economy, also sits in Category 3, alongside Gabon, the Postal Service charges less for the delivery of Chinese packages in the U.S. than it charges U.S. mailers for the same or similar services. For example, in 2016, a shipper in Beijing can send a 500g (1.1 lb) package to Chicago via China Post Airmail for \$11.52, whereas the Post Office charges a domestic mailer \$12.40 for carrying an identical weight package Priority Mail from San Francisco to Chicago. For China Post eBay ePacket shipments, the cost differential is even greater (see Appendix). This in turn means it is often possible for someone in China to send a package across the Pacific to anywhere in the 48 states for less than an American has to pay to send the same package

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<sup>20</sup> "China's E-commerce Revolution." *Morgan Stanley*. 13 Mar. 2015. Web.

<sup>21</sup> Dezan Shira & Associates. "Exporting to China: Import Tax Slashed in Cross-Border E-Commerce Zones." *China Briefing*. Ed. Rainy Yao. 2 Feb. 2016. Web.

<sup>22</sup> Xinhua. "Cross-border E-commerce to Boost Foreign Trade for China." *China Daily*. 16 Jan. 2016. Web.

<sup>23</sup> Kuo, Youchi. "3 Great Forces Changing China's Consumer Market." *World Economic Forum*. 4 Jan. 2016. Web.

<sup>24</sup> "China's E-commerce Revolution." *Morgan Stanley*. 13 Mar. 2015. Web.

*inside* the U.S.<sup>25</sup> This built-in cost advantage has enabled Chinese e-commerce firms to routinely offer free shipping to countries like the United States: an important plus in the highly competitive world of online shopping.<sup>26</sup>

The impact this has had in disadvantaging U.S. online retailers is readily apparent when we compare the costs of shipping small packages of electronics (2 kg or less) from Chinese e-commerce websites, with a similar U.S. retailer, namely Radio Shack.

For example, a standard multimeter for measuring electric voltage sells from Radio Shack for \$24.99.<sup>27</sup> From Deal Extreme, a Chinese e-commerce company, one can buy virtually the same multimeter for \$15.82.<sup>28</sup> With Deal Extreme's free shipping (since the postal rate it pays is so low) versus the \$5.95 Radio Shack has to charge, and a multimeter from Deal Extreme costs the customer only \$15.82, while Radio Shack charges \$30.94 — nearly double the amount.

Of course, some of that lower price reflects lower manufacturing costs in China. Yet looking at the example of an 8GB USB flash drive that sells for \$11.99 on the Radio Shack website<sup>29</sup> and almost the identical drive for only a dollar more (\$12.99) at another Chinese website, DinoDirect,<sup>30</sup> is instructive. Thanks again to the advantage of offering free shipping, DinoDirect can sell its flash drive to a U.S. customer at \$12.99, while U.S. shipping costs drives Radio Shack's price up to \$17.94.

The ways that free shipping from China skews the e-commerce playing field don't stop there. There is a soldering iron for electronics that actually costs less from Radio

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<sup>25</sup> "Terminal Dues in the Age of E-commerce." *Office of the Inspector General United States Postal Service*. Report Number. RARC-WP-16-003, pp. 10-12. 14 December 2016.

<https://www.uspsoig.gov/document/terminal-dues-age-e-commerce>

<sup>26</sup> See, e.g., the example in Copenhagen Economics, *The Economics of Terminal Dues: Final Report* (Sep. 30, 2014), pp. 45-46. This report was prepared for the Postal Regulatory Commission and is available from the Commission's website at [www.prc.gov](http://www.prc.gov).

<sup>27</sup> "17-Range Analog Multimeter." *RadioShack*. Web.

<https://www.radioshack.com/products/radioshack-17-range-analog-multimeter?variant=5717081349>.

<sup>28</sup> "LODESTAR LD3802A Handheld 2.0" LCD Digital Multimeter / Voltmeter / Thermometer- Orange Deep Grey." *DealExtreme*. Web. <http://www.dx.com/p/lodestar-ld3802a-handheld-2-0-lcd-digital-multimeter-voltmeter-thermometer-orange-deep-grey-237985#.V9Fp-5grK00>.

<sup>29</sup> "SanDisk Cruzer Glide 8GB USB Flash Drive." *RadioShack*. Cost on July 20, 2016.

<sup>30</sup> "8G/16G/32G Smart Phone Tablet PC USB Flash Drive OTG External Storage - DinoDirect Mobile Site." *DinoDirect*. Web. <http://m.dinodirect.com/product/8g-16g-32g-smart-phone-tablet-pc-usb-flash-drive-otg-external-storage-p42211540.html>. Cost as of July 2016.

Shack<sup>31</sup> than from the Chinese website DHGate,<sup>32</sup> namely \$14.99 versus \$17.53. The discriminating customer soon notices, however, that with DHGate's free shipping he will pay only \$17.53 buying his device from China, instead of the \$20.94 he'd have to pay Radio Shack when shipping is added in.

How important is this price differential? In Radio Shack's case, it may have been the margin between solvency and bankruptcy. Radio Shack's most loyal customers were buyers of small electronics parts for do-it-yourself projects — whether they bought them in the store or from Radio Shack's website.<sup>33</sup> Radio Shack's business model for staying in business depended on those 2 kg-or-less orders. Its declaration of bankruptcy in 2015<sup>34</sup> was due in part to the fact that it lost a major proportion of its customer base to websites originating in China — supported by the UPU's anti-competitive arrangement.

What's true for Radio Shack is undoubtedly also true for other U.S. online retailers — and the United States Postal Service has not been helpful in this regard. In 2010, in an alternative bilateral terminal dues agreement with China Post, the Postal Service established special rates and services for small packages originating from China, dubbed ePacket.<sup>35</sup> Under the agreement with China's state carrier, the Postal Service agreed to provide tracking and delivery confirmation as well as expedited delivery to customers in the U.S. The goal, according to a postal official, was “increasing international package volume for the Postal Service” — even though in 2014 the Postal Service collected only \$1.50 for delivering a 1-lb package from a foreign carrier, making it extremely difficult to cover its own costs.

The impact was sweeping. Between fiscal years 2011 and 2012, Chinese ePackets shipped into the U.S. under this program nearly tripled. The Postal Service's revenue increased, but the Postal Service's inspector general found that it was losing on average a dollar per incoming item, amounting to a \$29.4 million net loss in 2012.<sup>36</sup>

Yet while the Postal Service itself was losing money on ePacket, American eBay retailers were losing even more. Many were finding that the advantages Chinese online

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<sup>31</sup> "RadioShack 60W Soldering Iron." *RadioShack*. Web. <https://www.radioshack.com/products/radioshack-60w-soldering-iron?variant=5717846597>. Cost as of July 2016.

<sup>32</sup> "Electronics DIY Gas Soldering Iron Gun Blow Torch Cordless Solder Iron Pen MT-100 Tool Free Shipping." *DHGate*. Web. <http://www.dhgate.com/store/product/electronics-diy-gas-soldering-iron-gun-blow/192031722.html>. Cost as of July 2016.

<sup>33</sup> Sakraida, Lindsay. "Survey Says: RadioShack's Prices Are Too High & No One Shops Online." *DealNews*. 10 Mar. 2014. Web.

<sup>34</sup> Ruiz, Rebecca R., and Michael J. De La Merced. "RadioShack Files for Chapter 11 Bankruptcy After a Deal With Sprint." *The New York Times*. 5 Feb. 2015. Web.

<sup>35</sup> "The Postal Service Is Losing Millions a Year to Help You Buy Cheap Stuff from China." *The Washington Post*. 12 Sept. 2014. Web.

<sup>36</sup> U.S. Postal Service, Office of the Inspector General, "Inbound China ePacket Costing Methodology: Audit Report" (Feb. 25, 2014), p. 3.

companies were deriving from ePacket were driving them out of business. “I must say that it is simply an economic disaster for U.S. Sellers,” said one eBay member quoted in the Washington Post, “One product we sell for 2.00 with 2.59 shipping a Chinese company is selling for .99 with free shipping.”

As Washington Post reporter Jeff Guo put it, eBay sellers were running afoul of “an international treaty that makes it possible for an individual to send a pound of stuff from Hong Kong to [Washington] D.C. for less than it would cost to send the same package to, say, Seattle.”<sup>37</sup>

In July 2016, Ina Steiner, editor and publisher of EcommerceBytes.com, an online newsletter for e-commerce sellers, sent a letter to the members of the Postal Regulatory Commission,<sup>38</sup> which stated:

“Shipping is a major issue for our readers, and shipping costs directly impact their margins and profitability ... Knowing that domestic mailers are subsidizing foreign mailers who use the same postal infrastructure, but who do not contribute to the Postal Service’s institutional costs, is not only upsetting in principle; it harms many US merchants, particularly small online sellers.”

Steiner added, “The USPS Inspector General said in a December 15<sup>th</sup> [2015] report that inexpensive deliveries from China may potentially penalize domestic retailers. Based on my extensive knowledge of e-commerce as well as what I hear from online sellers, I believe that is absolutely the case.”<sup>39</sup>

It is not only small online retailers who feel the pressure — and fear the consequences — of the unfair advantage foreign e-commerce sellers enjoy because of UPU rules. In recent Congressional hearings, Amazon added its voice to the concerns that leaving the current rules in place will have a negative impact on its present and future business.

“Delivery is a very important part of the customer experience at Amazon,” Amazon’s Vice President for Global Public Policy Paul Misener told the House Subcommittee on Government Operations during hearings on fair competition in international shipping on June 16, 2015, “accordingly we maintain strong ties to postal operators around the world, including the U.S. Postal Service and China Post. [However] we have concerns

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<sup>37</sup> Guo, Jeff. “The Postal Service Is Losing Millions a Year to Help You Buy Cheap Stuff from China.” *The Washington Post*. 12 Sept. 2014. Web.

<sup>38</sup> Steiner, Ina. “Re: Docket IM2016-1.” Letter to The Postal Regulatory Commission. 21 July 2016. Natick, Massachusetts. Available from <http://www.prc.gov/dockets/doclist/IM2016-1/Comments/>.

<sup>39</sup> Steiner is referring to United States Postal Service, Office of the Inspector General, “Terminal Dues in the Age of E-commerce” (Dec. 14, 2015). Available from <https://www.uspsoig.gov/document/terminal-dues-age-e-commerce>.

about international postal agreements and their indirect effects on American businesses of all sizes.” Misener noted that extremely low bulk shipping rates were currently often cheaper from China to the U.S. than shipments between the U.S.’s 50 states.

He concluded, “For the sake of both effective competition in shipping and fairness to American seller businesses, the UPU terminal delivery compensation system and current bilateral agreements [such as ePacket] between the USPS and key foreign postal operators such as China Post must be reformed.”<sup>40</sup>

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<sup>40</sup> United States. Cong. House. Committee on Oversight and Government Reform. *Hearing on Fair Competition in International Shipping. June 16, 2015*. 114th Cong. 1st sess. Washington: GPO, 2015 (testimony of Paul Misener, Vice President for Global Public Policy, Amazon.com). PDF file.

### ***Multiple Economic Distortions That Flow from UPU Terminal Dues***

**T**o review: the UPU sets the rules for the exchange of mail between its member countries. According to these rules, post offices compensate each other for the cost of delivering inbound international mail. Rates for the delivery of “letter post” mail — documents and packages weighing up to 2 kg (4.4 lbs) — are called “terminal dues” and established in the Universal Postal Convention that the UPU revises and adopts every four years.<sup>41</sup> Post offices may also agree among themselves to different compensation rates, but inevitably alternative rates are heavily influenced by the default UPU rates. So, for example, when the Postal Service receives a document or small package (less than 2 kg) from the post office in Hong Kong or Germany for delivery to an address in Chicago, the Postal Service charges the origin post office “terminal dues” (or an agreed alternative rate close to UPU terminal dues) to deliver it in Chicago. That rate is below the out-of-pocket cost incurred by the Postal Service and even further below the equivalent rate that the Postal Service would charge a domestic mailer.

To allocate a resource such as mail delivery in a competitively neutral manner, rates for delivery of inbound international mail should be set to match the rates of domestic mail for similar services. This would ensure that a German, Canadian, or Chinese e-commerce retailer pays no more or less than his American counterpart for Postal Service delivery of the same package.

In its current form, the UPU system causes distortions in international postal delivery services because it systematically leads to substantial undercharging for the delivery of inbound international mail by industrialized countries (and some other countries). The UPU system also requires some post offices to subsidize others. (Under the current system, fifteen countries end up paying almost the entire net bill for these financial transfers between countries).<sup>42</sup> These are costs that have to be passed on to domestic customers and/or taxpayers. The U.S. Postal Service is forecasted to join this club of “net losers” in the 2018-2021 period, if it is not already a member.<sup>43</sup>

As outlined in Section II, China in particular has taken advantage of this system, on a scale that has given birth and sustained an entire industry, namely Chinese e-commerce. The same is true to a lesser degree for Hong Kong and Singapore. In the past few years e-commerce parcels from these three post offices have increased enormously, perhaps by as much as 100 percent or more each year, although firm data are lacking.

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<sup>41</sup> Terminal dues (and inward land rates for parcel post) only compensate for local or “last mile” delivery costs. The costs of long distance transportation within the destination country are compensated by other UPU fees.

<sup>42</sup> Copenhagen Economics, *Quantification of Financial Transfers*, p. 9.

<sup>43</sup> Okholm et al, “Forecast e-commerce impact on international subsidies from Terminal Dues,” p. 9.

In short, terminal dues impose a burden on domestic mailers who have to make up the discounts their Posts are forced to give to foreign mailers. In the U.S., the bottom line is that American consumers and retailers are unwittingly subsidizing foreign competition.

The UPU terminal dues system also produces distortions in the outbound postal market as well as the inbound market. The Postal Service sets postage rates for bulk outbound mail services for commercial mailers at levels that are close to terminal dues plus the cost of international transportation. Because terminal dues in most industrialized countries are set below cost, this means that U.S. commercial mailers are getting a service that is priced below the true cost of production. Good for them, but bad for the U.S. private carriers that provide competing international transportation services. At the same time, individual outbound mailers face substantially higher international postage rates, which may or may not benefit from artificially low terminal dues.

These several distortions affect different groups of Americans differently. American merchants are harmed by the underpricing of Postal Service delivery for foreign e-commerce packages. At the same time, American buyers of foreign e-commerce merchandise benefit. U.S. commercial mailers benefit if postage rates for outbound bulk mail are set below actual costs. Domestic U.S. mailers, however, are paying a little bit more to subsidize this general underpricing of international mail services. In both inbound and outbound markets, however, competing American air carriers and freight forwarders are harmed. They cannot compete in the transportation portion of the international postal market if the destination Post will not give them the same delivery rates as it gives the origin Post.

These various distortions do not truly offset because the groups that are harmed are not the same as those who benefit. Nonetheless, it is possible to roughly estimate the “net financial transfer” for a country as a whole. The costs associated with these price distortions are considerable. In December 2015, Copenhagen Economics, an independent Danish consulting firm, published a report for the Postal Regulatory Commission on the net financial transfers between 154 post offices worldwide, because of UPU rules. It estimated that in 2014 the net transfer totaled \$1.4 billion, with about 70 percent of this net transfer due to terminal dues for small packages. Almost all the net losses fell on just 15 post offices and their mailers.<sup>44</sup>

Through disparate pricing, the UPU terminal dues system creates opportunities for participants to turn a profit by bypassing the system, and the effort to prevent bypass has led to even more anti-competitive measures. For example, Posts can compete with each other as gateways into the international postal system by offering to give all customers, not just their own citizens, the benefits of low terminal dues rates. This possibility has, for example, induced some large U.S. mailers to transmit their international mail to such countries as the Netherlands for postal distribution to European addressees. This practice is called “re-mail.” Another way to bypass the terminal dues system is for Posts to open offices in each other territories — called “extraterritorial offices of exchange” or “ETOEs” — and compete directly for outbound

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<sup>44</sup> Copenhagen Economics, *Quantification of Financial Transfers*, p. 8-9.

international mail. As Deputy Assistant Attorney General Donna Patterson of the Antitrust Division of the Justice Department explained to Congress in 2000, such competition among Posts “has provided consumers with greater options in mail delivery, and significant benefits in the price and quality of international mail service.”<sup>45</sup> In response, the UPU has adopted a series of measures to restrain development of remail and ETOEs. The objective is to ensure that each Post has an advantage in the market for outbound mail originating its national territory. Such provisions, however, appear to be contrary to the postal laws and at a minimum run counter to the spirit of antitrust policy in most developed countries, including the United States and the European Union.

In summary, the UPU has skewed both terminal dues and international competition to the advantage of some Posts and to the disadvantage of other Posts, domestic merchants, and private carriers.

During her testimony to the Subcommittee on Postal Service of the House Government Reform Committee, Ms. Patterson went on to say, “We are pleased with the concession the U.S. Delegation obtained at the Beijing Congress [of the UPU] on terminal dues reform.” That was in 2000: there has been little serious reform in the intervening sixteen years. A fair terminal dues structure aligned with domestic postage rates, regardless of country, would eliminate most, if not all, the distortions in the present system.

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<sup>45</sup> United States. Cong. House. Committee on Oversight and Government Reform. *Hearing on International Postal Policy. March 9, 2000*. 106th Cong. 1st sess. Washington: GPO, 2000 (testimony of Donna E. Patterson, Deputy Assistant Attorney General, Antitrust Division, U.S. Department of Justice). PDF file.

## ***Terrorism and the Evolution of Sophisticated Customs and Security Controls for International (Non-Postal) Packages***

**T**he terrorist attacks on the United States on September 11, 2001, prompted Congress, in the Trade Act of 2002, to require carriers to provide U.S. customs authorities with electronic data describing all cargo to be brought into or sent from the United States prior to the arrival or departure of the cargo.<sup>46</sup> In December 2003, the Department of Homeland Security implemented this requirement by adopting the Automated Manifest System (AMS), which defines a comprehensive electronic manifest which must be submitted by air carriers and other parties either upon departure from a foreign airport, or four hours before arrival in the U.S., depending on the port where the cargo is embarked.<sup>47</sup>

The Trade Act of 2002 did not, however, require the international postal system to file advance electronic manifest data for postal items arriving in the U.S. The act provides that, "*With respect to requirements imposed on carriers, the Secretary, in consultation with the Postmaster General, shall determine whether it is appropriate to impose the same or similar requirements on shipments by the United States Postal Service. If the Secretary determines that such requirements are appropriate, then they shall be set forth in the regulations.*" Fourteen years later, Customs and Border Protection (CBP) has still not extended the advance electronic manifesting requirements to inbound international mail.

In 2010, another terrorist incident prompted an extension of data-filing requirements in the U.S. On October 29, 2010, explosives were discovered in two UPS packages collected in Yemen for delivery to synagogues in Chicago.<sup>48</sup> The bombs were manufactured by an Al Qaeda cell in Yemen which disguised the bombs as printer ink cartridges. Security authorities were tipped off to the presence of the bombs in the UPS system. Because express carriers like UPS electronically track all shipments, security authorities could "go straight to the illicit cargo."<sup>49</sup> Nonetheless, the threat from bombs in relatively small packages was dramatically highlighted.

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<sup>46</sup> Section 343 of the Trade Act of 2002, enacted by Pub. L. 107-210, div. A, title III, Sec. 343(a), (c), Aug. 6, 2002, 116 Stat. 981, 985, and amended by Pub. L. 107-295, title I, Sec. 108(b), Nov. 25, 2002, 116 Stat. 2089 and by Pub. L. 109-59, title XI, Sec. 11165(a), Aug. 10, 2005, 119 Stat. 1976. The title of Section 343 explains its purpose: "Mandatory advanced electronic information for cargo and other improved customs reporting procedures." Section 343, as amended, is set out as a note to 19 U.S.C. § 2071.

<sup>47</sup> See 19 C.F.R. §122.48a.

<sup>48</sup> Wassef, Khaled. "Timeline of Yemen Bomb Plot." *CBSNews*. 30 Oct. 2010. Web.

<sup>49</sup> Soltis, Andy. "Bomb Tip from Qaeda Traitor." *New York Post*. 02 Nov. 2010. Web; Shane, Scott. "Qaeda Branch Aimed for Broad Damage at Low Cost." *The New York Times*. 20 Nov. 2010. Web; "Profile: Saudi Interior Minister Prince Mohammed Bin Naif." *Asharq Al-Awsat*. 6 Nov. 2012. Web.

The Yemeni incident prompted the Department of Homeland Security to adopt a voluntary program in 2012 called the Air Cargo Advance Screening or ACAS program.<sup>50</sup> Under ACAS, air carriers are encouraged to provide CBP with a basic set of eight security-related data on shipments destined for the U.S. *prior to consolidation and loading the cargo on an aircraft*. The objective is to give CBP an opportunity to issue a “do not load” order to the carrier. ACAS is still a pilot program. The first participants were the express carriers, including FedEx and UPS. The program has been extended to include passenger airlines and freight forwarders. Although ACAS is still only a pilot program, most observers have branded it a success, and in July 2016 CBP extended the program to July 26, 2017.<sup>51</sup> CBP intends to make ACAS mandatory when it is satisfied that it can be implemented smoothly. The European Commission and Canada are pursuing similar programs.<sup>52</sup> The Posts do not participate in the ACAS program.

The UPU Convention does not address the customs entry of postal shipments except to say that Posts “shall be authorized to submit items to customs control, according to the legislation of those countries.”<sup>53</sup> At the same time, the Convention exempts Posts from liability under national customs laws.<sup>54</sup> This relieves the Posts of a crucial incentive to pressure each other for complete and accurate customs and security data.

The special customs procedures for postal shipments developed by the UPU are the result of Regulations issued by the Postal Operations Council (POC). The POC is a permanent committee of 40 Posts dominated by the largest and most commercially active Posts. The POC has adopted two simplified “customs declarations” which are to be completed by the mailer and affixed to the postal envelope or package. The simpler form, the CN 22 form, is a 2.5 inch by 3 inch green label that has spaces for a description of the item, the weight, and the value. The CN 22 is used for shipments valued less than about \$400. A more detailed form, the CN 23, is used for higher value shipments. Since the CN 22 and CN 23 are applicable to all postal shipments worldwide, the POC has, in essence, adopted for Posts (and only for Posts) a simplified customs entry procedure that is applicable in all countries. This replaces the patchwork of national customs regulations that other cargo carriers must contend with. Under the UPU Constitution, POC Regulations are binding on national governments.

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<sup>50</sup> "Extension of the Air Cargo Advance Screening (ACAS) Pilot Program." *Federal Register*. 21 July. 2016. Web.

<sup>51</sup> "Extension of the Air Cargo Advance Screening (ACAS) Pilot Program." *Federal Register*. 21 July. 2016. Web.

<sup>52</sup> "Air Transportation." *Government of Canada*. 18 July. 2012. Web.

<sup>53</sup> Universal Postal Convention 2012, art. 20. The corresponding provision in the Universal Postal Convention 2016 is unchanged.

<sup>54</sup> Universal Postal Convention 2012, art. 24(3) (“Member countries and designated operators shall accept no liability for customs declarations in whatever form these are made or for decisions taken by the Customs on examination of items submitted to customs control”). The corresponding provision in the Universal Postal Convention 2016 is unchanged.

In 2012, the UPU Congress in Doha added a new provision of the Convention to forestall the development of multiple national security regulations like ACAS. Article 9 of the 2012 Convention accepts that postal shipments should eventually be subject to advance electronic data requirements, but gives the UPU a substantial role in deciding what and when.

1. Member countries and their designated operators shall observe the security requirements defined in the UPU security standards ... This strategy shall, in particular, include the principle of complying with requirements for providing electronic advance data on postal items identified in implementing provisions ... adopted by the Council of Administration and Postal Operations Council. ...

2. Any security measures applied in the international postal transport chain must be commensurate with the risks or threats that they seek to address, and must be implemented without hampering worldwide mail flows or trade by taking into consideration the specificities of the mail network. Security measures that have a potential global impact on postal operations must be implemented in an internationally coordinated and balanced manner, with the involvement of the relevant stakeholders.

Armed with these legal provisions, the UPU has resisted the application of national customs and security regulations to postal shipments. In 2014, as part of a modernization of its customs and security programs, the European Union proposed to require post offices to provide advance electronic security data similar to that required in the U.S. by ACAS beginning on May 1, 2016. The EU program would apply only to EMS and parcel post shipments; submission of similar data for the much larger volume of small packets would be required at a later date. The UPU protested to EU against this program arguing that “[t]he UPU is the sole specialized agency recognized by the United Nations for action in the field of international postal services,” and urged the EU to delay the application of security requirements to postal package until “a global consensus and solutions can be implemented” with “proper transitional measures.”<sup>55</sup> The EU has postponed the application of customs and security requirements to postal shipments, apparently until at least the end of 2020.

At the same time, under pressure for aviation security and customs authorities, both national and international, the UPU is gradually taking steps toward providing at least some advance electronic data to customs and security authorities. Over several years, the POC has developed a “roadmap” for implementing a “Postal Model” for advanced electronic data to be provided by Posts.<sup>56</sup> The core data to be conveyed is defined by the

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<sup>55</sup> Letter from Pascal Clivaz, Deputy Director General, UPU, to Pierre Moscovici, Commissioner, Economic and Financial Affairs, Taxation and Customs, European Commission, dated 11 December 2014. See UPU, International Bureau, EMIS 2014/98 (Dec 15, 2014), Annex 3.

<sup>56</sup> The International Air Transport Association, an association of international airlines, has objected to this model as too burdensome for the air carrier. UPU, Postal Operations

paper “customs declarations” — the simple CN 22 form and more detailed CN 23 form. According to the Postal Model, the origin Post would assemble the CN 22 and CN 23 information provided by mailers into an electronic file. The data file would be limited to postal shipments containing “goods”; the POC has exempted letters, postcards, and printed papers from national advance electronic data regulations.<sup>57</sup> The origin Post would be responsible for providing basic ACAS-like security data to customs (or the destination Post) in the destination country while the air carrier (or the destination Post) would be responsible for filing the more detailed AMS-like customs data with customs in the destination country based on the shipment-level data supplied by the origin post office. In February 2016, the UPU approved a version of the roadmap that calls for the introduction of the Postal Model over four years, from early 2016 through the end of 2019.<sup>58</sup>

The provision of such data would be an important step forward, but it would be a far cry from placing the Postal Service in the same legal position as private carriers when it comes to import of international packages. Unlike private carriers, the Postal Service would not be required to assume the obligations and liabilities of the “nominal consignee” and (for most shipments) “importer of record.”

In the United States, the disparity between U.S. legal requirements and UPU practices was sharpened by enactment of the Postal Accountability and Enhancement Act (PAEA) in 2006. With respect to the application of customs and security laws to international postal shipments, the PAEA declared:

The Customs Service and other appropriate Federal agencies shall apply the customs laws of the United States and all other laws relating to the importation or exportation of such shipments [competitive postal shipments] in the same manner to both shipments by the Postal Service and similar shipments by private companies.

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Council, POC C1 CG 2015.2 Doc 5c and 5d. Negotiations between IATA and the UPU are continuing.

<sup>57</sup> In February 2016, the POC adopted a new regulation, RL 104bis, which provides, “Letter-post items containing goods may be subject to specific import customs- and security-based requirements for providing electronic advance data as referred to in article 9.1 of the Convention. *Letters, postcards, printed papers (other than books) or letter-post items containing correspondence or items for the blind, which are not subject to customs duties, shall be exempted from these requirements* [emphasis added].”

<sup>58</sup> UPU, Postal Operations Council, POC 2016.1 Doc 10m Annex 1 (Feb.3, 2016) (Roadmap for Implementing the UPU Electronic Advance Data Global Postal Model (Version 2016\_1\_21)).

The Secretary of State was further directed to exert maximum efforts “to encourage the governments of other countries to make available to the Postal Service and private companies a range of nondiscriminatory customs procedures.”<sup>59</sup>

Unlike the Trade Act of 2002 and other initiatives of CBP, the goal of the PAEA was not to prevent acts of terrorism but to ensure fair competition and economic efficiency. Nonetheless, the requirement of equal application of customs and security laws serves the same end. The customs and security controls developed for cargo generally and private package delivery services should apply equally to packages conveyed by the international postal system since potential terrorists will send packages by whatever means is least protected.

As of today, notwithstanding the requirements of the PAEA, the customs and security controls for packages entering the U.S. — including identical packages arriving on the same aircraft — are vastly different depending on whether the packages are conveyed by the international postal system or not (with a handful of exceptions).<sup>60</sup> As provided in the ACAS program, express carriers like FedEx and UPS and other cargo carriers electronically transmit basic security data to CBP before they load a package into a plane bound for the U.S. Foreign Posts provide no pre-loading data. As required by the Automated Manifest System, express carriers and other cargo carriers electronically transmit to CBP in advance of arrival in the U.S. an electronic manifest that provides the detailed information needed to make the customs entry for each package conveyed.

Neither the foreign Posts nor the Postal Service provide any advance electronic data on packages conveyed by the international postal system. On arrival, postal shipments are presented to CBP with paper CN 22 or CN 23 affixed and no electronic summary. The Postal Service does not make an entry for any shipments. In principle, CBP is supposed to search through these shipments — the Postal Service imports hundreds of thousands of documents and packages each day — and identify shipments which may violate U.S. law or require payment duty. If CBP finds a package that requires customs entry, a CBP official completes a “mail entry” unless the value of the package exceeds \$2,500. In practice, it is simply impossible for CBP to physically inspect any more than a tiny fraction of postal shipments.

In essence, CBP has no information on what the international postal stream is bringing into the country. In the wake of 9/11 and the 2010 Yemeni incident, CBP has developed sophisticated electronic data filing requirements and analysis procedures to counter use of the international package delivery system by terrorists. Yet these controls are not applied to the largest flow of packages entering into the U.S.: the packages shipped via

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<sup>59</sup> 39 U.S.C. § 407.

<sup>60</sup> Representatives of CBP told the commission that it is conducting trials with fourteen foreign posts who are providing shipment-level electronic data for some EMS shipments in advance of arrival in the U.S. CBP did not offer details of this program, but it does not appear to impose the same requirements on postal shipments as privately carried shipments. In any case, EMS shipments comprise only a tiny fraction of all postal shipments imported into the U.S.

the international postal system. Instead, the U.S. has, to an unfortunate degree, ceded control over the flow of international postal packages to the UPU's Postal Operations Council, a committee of 40 commercially minded postal officials with the authority to legislate international regulations binding on the U.S.

## ***The Threat of Illicit Drugs in International Postal Packages***

*We cannot allow our Federal Government and the U.S. Postal Service to become the drug carriers of choice for our drug dealers.*

—Rep. John Mica (R-FL), Subcommittee on Criminal Justice, Drug Policy, and Human Resources, Committee on Government Reform, May 26, 2000.

**O**n Thursday, November 3, 2016, Park City, Utah, police confirmed that two local 13-year-old boys who had died suddenly within days of one another had overdosed on a synthetic opioid known as “pink” or U-47700. Search warrants revealed that the two teens had ordered the substance from China and had it mailed to a friend’s house because the boys’ parents were regularly screening the mail for drugs. According to the Salt Lake Tribune, their friend had received the package from mainland China, and it contained “a clear bag with a white powder substance.”

While the coverage has not specified how the package was mailed from China, it may have been delivered to Park City by the U.S. Postal Service.<sup>61</sup>

Although the collection and analysis of advance electronic data for international packages was originally introduced to support counterterrorism initiatives, it has become increasingly apparent that this information is also needed to fight what may be an even more deadly threat: the traffic in illicit drugs.

According to the Centers for Disease Control and Prevention, more than 28,000 people died of opioid drug overdoses in 2014, although many experts believe the actual number is much higher.<sup>62</sup>

For decades the illegal drug trade has had a devastating impact on American communities, families, schools, and individuals. Recently the problem has become even more acute, thanks to the growing availability of synthetic drugs that mimic the effects of illicit substances such as heroin and marijuana, but with far more dangerous and lethal effects. In many cases these synthetics are made with chemicals that can be cheaply purchased online. Despite Rep. Mica’s warning more than sixteen years ago, there is a palpable risk that use of the international postal system to transport illicit drugs may have, if anything, grown worse.<sup>63</sup>

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<sup>61</sup> Jessica Miller, “Medical Examiner: Two 13-year-old Utah boys died from synthetic opioid “Pink”, *The Salt Lake Tribune*, November 3, 2016. <http://archive.sltrib.com/story.php?ref=/news/4541156-155/medical-examiner-two-13-year-old-utah-boys.it>

<sup>62</sup> "Injury Prevention & Control: Opioid Overdose." Centers for Disease Control and Prevention. <https://www.cdc.gov/drugoverdose/>

<sup>63</sup> United States. Cong. House. Committee on Oversight and Government Reform. *Hearing before the Subcommittee on Criminal Justice, Drug Policy, and*

Senator Ron Johnson (R-WI) expressed this concern in an April 2016 Homeland Security and Governmental Affairs Committee roundtable: “Once drugs are purchased online, they are mailed through foreign postal systems, [and] delivered within the United States by the U.S. Postal Service.”<sup>64</sup>

Because there is no standard system of providing manifests on contents for customs purposes, there is no system for preventing the mail’s use for illegal commodities. As Senator Tom Carper noted in the same April 2016 roundtable, “while the U.S. Postal Service provides advance electronic data to foreign countries about mail originating in the United States, foreign nations do not always reciprocate and provide us with similar information that we need. This failure to share makes it harder for CBP to do its job when mail and mail cargo arrive here.”<sup>65</sup>

As noted by Senator Ron Johnson, while numerous federal agencies are working hard to prevent illegal drugs from reaching America, “the U.S. Postal Service is compelled by treaties on international mail exchange to deliver mail on behalf of foreign posts. Because they cannot control which individuals use these international services, the Postal Service can become an unwitting drug courier.”

In written testimony submitted to the Commission, Senator Johnson explained that his committee has held eighteen sets of hearings on border security, four of which centered on the current opioid epidemic sweeping the country. What they found was that “numerous Federal agencies, including the Drug Enforcement Agency and Customs and Border Protection, agree that illicit goods, including deadly chemicals and counterfeit goods, are primarily produced in and exported from a small number of countries, including China and India.”

LegitScript, a verification and monitoring service for online pharmacies, estimates that there are 30,000 to 35,000 illegal online pharmacies operating at any one time.<sup>66</sup> How many of these illicit drugs are imported via the international postal system? In 1999, of the 200 billion pieces of mail (domestic and international) handled by the Postal

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*Human Resources*. May 26, 2000. 106th Cong. 2nd sess. Washington: GPO, 2015 (testimony of Rep. John Mica). PDF file.

<sup>64</sup> United States. Cong. Senate. Committee on Homeland Security and Governmental Affairs. *Roundtable: Preventing Drug Trafficking through International Mail*. April 19, 2016. 114th Cong. 2nd sess. Video file available from the committee. Web.

<sup>65</sup> United States. Cong. Senate. Committee on Homeland Security and Governmental Affairs. *Roundtable: Preventing Drug Trafficking through International Mail*. 19 Apr. 2016. 114th Cong. 2nd sess. (testimony of Senator Tom Carper). Video file available from the committee. Web.

<sup>66</sup> The Internet Pharmacy Market in 2016: *Trends, Challenges, and Opportunities*. LegitScript. January 2016. <https://safemedsonline.org/wp-content/uploads/2016/01/The-Internet-Pharmacy-Market-in-2016.pdf>

Service, some 15,000 pounds of illegal drugs were seized.<sup>67</sup> Nearly all that illegal trade came from foreign sources. The big concern at the time was ecstasy, one of the first notorious synthetic drugs. Yet even then the sheer volume of illegal drugs entering the U.S. by mail was making the task of monitoring and intercepting those drugs extremely difficult. As Ms. Betsy Durant, Director, Office of Trade Programs and Office of Field Operations at the U.S. Customs Service, told the House members in the 2000 hearing, “Customs is feeling pretty overwhelmed on all fronts.”<sup>68</sup>

Ms. Durant’s comments were made prior to the explosive growth in international e-commerce, which, it seems reasonable to surmise, has made the problem even larger. While exact numbers are not known, Brenda Smith of CBP told the commission that her agency seized 35 tons of illegal drugs in the mails last year alone, and more than 11,000 shipments of counterfeit goods.<sup>69</sup>

A good example of the heightened risk today is fentanyl, which is fifty times more potent than heroin and killed twice as many people in 2013 than the year before. In fact, the total number of drug-related deaths increased by 5,400 people in 2015 as fentanyl jumped onto the list of the top five most lethal drugs — a drug which also killed the rock star Prince.<sup>70</sup> A recent front-page article in *The Wall Street Journal*, based on a recent internal U.S. Drug Enforcement Administration intelligence briefing, concluded that fentanyl is arriving in the U.S. as part of “a vast drug-distribution network beginning in China that feeds lethal fentanyl to the Americas.”<sup>71</sup>

As *The Wall Street Journal* reported, much of the trafficking of fentanyl flows from China to Mexican production labs on the country’s Pacific coast. But some also involves small-time traffickers here in the U.S. buying fentanyl and its analog drugs online. Whether on a small or grand scale, this illicit traffic often comes via foreign posts and the Postal Service.

Why would dealers in fentanyl and similar drugs use the international postal system to ship their goods to the United States? These drugs are so concentrated that even

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<sup>67</sup> United States. Cong. House. Committee on Government Reform. *Drugs in the Mail: How Can It Be Stopped?* May 26, 2000. 106th Cong. 2nd sess. Washington: GPO, 2000 (testimony of Rep. Jim Turner). PDF file.

<sup>68</sup> United States. Cong. House. Committee on Oversight and Government Reform. *Hearing before the Subcommittee on Criminal Justice, Drug Policy, and Human Resources. 26 May 2000.* 106th Cong. 2nd sess. Washington: GPO, 2015 (testimony by Betsy Durant, Director, Office of Trade Programs and Office of Field Operations at the U.S. Customs Service). PDF file.

<sup>69</sup> It is a reasonable inference that this represents a small proportion of total shipments of both.

<sup>70</sup> Goodman, Brenda, MD. “Fentanyl Overdose Deaths Double in a Year.” *WebMD*. 20 Dec. 2016. <http://www.webmd.com/mental-health/addiction/news/20161220/fentanyl-overdose-deaths-double-in-a-year>.

<sup>71</sup> Whalen, Jeanne, and Brian Spegele. “The Chinese Connection Fueling America's Fentanyl Crisis.” *The Wall Street Journal*. 23 June. 2016. Web.

quantities small enough to ship in large envelopes or small packages are commercially valuable. For example, a single kilogram of pure fentanyl can produce up to 100 million recreational doses, or 500,000 lethal doses, which means a packet of only a few grams can service a drug dealer's entire clientele. The international postal system offers an almost risk-free means of transporting such shipments to the U.S. CBP has no way to monitor such shipments as they cross the border. And unlike private carriers, the international postal system produces no "paper trail" that can be used to investigate past shipments — a major stumbling block for law enforcement agencies. Even if an illicit shipment is discovered in the mail, there is almost no chance of finding the foreign mailer.

There is no way to survey those who traffic in illegal drugs like fentanyl to find out how they ship their goods.<sup>72</sup> However, between January 2015 and May 2015 LegitScript did a study of a closely related issue, the shipping method used in 29 test buys from illegal online pharmacies.<sup>73</sup> LegitScript found that all the purchases were being shipped into the U.S., yet only two of the illegal pharmacies originated in the U.S.

The other 27 test buys originated from foreign countries. All sellers used the national postal services to move the illegal drugs. "In no case did US Customs stop or intercept the package," the study's researchers concluded. They note, "In all cases, the US Postal Service provided the distribution once the drugs reached US soil" — without asking what was contained in the packages.

The report also estimated that of the 30,000 to 35,000 websites selling prescription drugs, 5,000 to 10,000 specialize in designer drugs. Approximately 95-97 percent of those Internet pharmacies operate illegally — and 90 percent specifically target the U.S.

Under UPU terminal dues rules (see Section III) those foreign illegal pharmacies also get a discount on their postage. This means that the international postal system is both providing transportation for the illegal prescription drugs, while also subsidizing the trade. Just as Chinese e-commerce firms have taken advantage of the UPU loophole to build their businesses, so have traffickers in illegal prescription drugs.<sup>74</sup>

In sum, although the volume of illegal drugs in the international postal system is unknown, the extreme risk to the health of Americans is apparent. The advance electronic data filing requirements that CBP has developed to prevent the use of international package delivery services by terrorists is also needed to fight the international traffic in illegal drugs.

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<sup>73</sup> *Analysis of Rogue Internet Pharmacy Shipping Methods. LegitScript. July 2015. PDF file.*

<sup>74</sup> Green, J.J. "'Huge Security Gap' Lets Dangerous Packages Enter US through Postal System." *Washington's Top News*. 07 Sept. 2016. Web.

## ***Lost Customs Duties on International Postal Packages***

**T**he absence of reliable data on packages imported via the international postal system also adversely affects the revenue of the U.S. government. As a matter of national law, the United States has the right to impose customs duties on certain goods entering the country from foreign countries — although most industrialized countries also exempt goods below a certain value (*de minimis* value) from those duties. For shipments with a value higher than the *de minimis* level, the CBP collects an amount of duty determined by Congress that varies with the type of good imported.

Duty is payable regardless of whether the shipment arrives by post or by private carrier. For postal packages, however, CBP is restricted by the lack of advance electronic data. Duty is collected only when a CBP inspector happens to discover a dutiable package in a vast sea of non-dutiable documents and low-value packages. Customs inspection of international mail deliveries is a matter of physical checks and selective searches based on the country of origin, size of package, or other extrinsic factors. The process is unsystematic and even haphazard, due to the volume of packages, especially small packages, entering the U.S. by mail, and the volume of non-postal items customs inspectors also have to handle.

In the unlikely event that a CBP inspector discovers a dutiable postal package, because of the due to UPU Convention rules, neither the sender nor the destination post office (nor anyone else) is liable for incomplete or inaccurate information in the UPU customs form attached to the package.

Although the problem is apparent, no one really knows its extent. Given the explosive growth of volume in international e-commerce, however, potentially large sums of customs duties are not collected. One recent study casts some light on this issue.

The consultancy firm Copenhagen Economics studied the shipment of international packages to the United States, by value and type of merchandise.<sup>75</sup> Their report found that exact data on the volume of packages imported via the international postal system into the U.S. are not publicly available. Nonetheless, the study estimated that “at a minimum, 179 million ‘non-letter’ items enter the U.S. annually” (CBP’s estimate presented to the commission was slightly higher). These items typically include music and video DVDs and CDs, medicines and dietary supplements, jewelry and small electronics items — the common commodities of today’s e-commerce.

The report also found that “the US Postal Service will likely receive a greater share of non-letter to letter inbound postal items than many” of the 49 countries examined in another unrelated UPU survey. As of 2012 there were more than 34 million Americans engaged in cross-border e-commerce transactions, with that number forecast to grow to

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<sup>75</sup> Copenhagen Economics. “Private Express Carriers’ vs Posts’ Treatment of Packages Inbound to the US: Security Risks and Customs Concerns.” 2015. PDF file. In this study, “non-letters” were defined as “pieces that are larger than letter mail, and include both ‘flats’ and ‘packets’ as defined by the UPU.”

42 million by 2018 — with more than \$80 billion being spent on imported e-commerce goods.

Furthermore, Copenhagen Economics' researchers found that, in a series of test shipments for which entry and duty payments were required, international express carriers submitted 98 percent of the necessary customs declarations to CBP, but not a single customs declaration was made on packages that were shipped into the U.S. via the international postal system.

The report determined that “[t]he absence of dues and fees collected on postal packages inbound into the U.S. translates to a loss estimated at over \$1.06 billion annually in public sector income [in 2014].” Since the *de minimis* exemption has been raised from \$200 to \$800, that almost certainly overstates the amount of lost customs duties in the future. Nonetheless, lost customs duties do represent income that could be used to strengthen CBP’s inspection process, or help fund a more efficient electronics system for identifying and tracking international packages entering the U.S.

## **Conclusion of the 2016 Universal Postal Convention**

On October 8, 2016, while this report was being prepared, the plenipotentiary delegates to the UPU Congress in Istanbul signed a new Universal Postal Convention that will be effective from January 1, 2018, through December 31, 2021. The State Department signed for the United States. The 2016 UPU Convention makes small changes in the terminal dues system and adds new restrictions on ETOE competition. The customs and security provisions in the 2016 Convention are unchanged from the 2012 Convention.<sup>76</sup>

As required by the PAEA, the State Department asked the Postal Regulatory Commission to review the new terminal dues agreement before the Istanbul Congress convened. The PRC is required to determine whether the terminal dues that are to be adopted by international agreement are “consistent with the standards and criteria established by the Commission under Section 3622” of U.S. postal laws, title 39 of the U.S. Code, Section 3622 which states that the PRC must “establish ... a modern system for regulating rates and classes for market-dominant products.”<sup>77</sup> The PRC defines the term “market-dominant product” to include all inbound letter post mail. Hence, the task of the PRC was to decide whether terminal dues proposed for 2016 UPU Convention were consistent with the mandate in Section 3622.

On August 31, 2016, after soliciting public comments, the PRC transmitted its views to the State Department. The PRC stated that it was unable to decide whether the proposed terminal dues are consistent with U.S. postal law because the four Commissioners were divided 2 to 2 (there is one vacancy at the PRC). This non-decision was accompanied by two well-reasoned letters written by Acting Chairman Robert Taub and Commissioner Mark Action, both of whom found the proposed terminal dues inconsistent with the criteria of U.S. postal laws.

“Even if the Postal Service *projections* for proposed terminal dues rates are fully accurate for the first time in history,” Acting Chairman Taub wrote, “domestic mailers will continue to subsidize the entry of Inbound Letter Post by foreign mailers.” He noted that the “exploding” volume of small packets means that in effect the Postal Service is subsidizing e-commerce from foreign countries thanks to non-compensatory terminal dues. He added, “Simple improvement of existing below cost rates to ‘less below’ cost rates [the gist of the proposed UPU changes] is not a foundation for declaring proposed terminal dues rates consistent with the law in 2016.” Taub also found the terminal dues were inconsistent with no less than seven of the nine objectives in 39 U.S.C. § 3622, from the need “to maximize incentives to reduce costs and increase efficiency” and “assure adequate revenues, including retained earnings, to maintain

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<sup>76</sup> UPU, 2016 Istanbul Congress, Draft Acts Doc 4, [2016] Universal Postal Convention, arts. 8 (postal security), 12 (re-mail), 12bis (use of UPU documentation by ETOEs), 19 (postal customs), 22(3) (non-liability under national customs laws), 27-29 (terminal dues), 31 (inward land rates).

<sup>77</sup> 39 U.S.C. § 407(c)(1).

financial stability” to “enhance mail security and deter terrorism.” Taub concluded, “I am compelled to find the terminal dues proposals inconsistent with the law.”

Commissioner Mark Acton concurred: “It is my view that as a function of emergent global market realities alone, these [UPU] proposals are becoming increasingly problematic with respect to meeting the relevant statutory objectives and factors.” He suggested, “If a more market-centric resolution cannot be brokered within the UPU, perhaps a coordinated member state initiative without the UPU offers a brighter, longer term prospect toward driving fuller cost coverage and reducing unfair trade distortions.”

As of yet, the parties who have supported the new UPU terminal dues agreement—the Postal Service, State Department, and two PRC Commissioners—have not offered formal analysis to support the proposition that new rates are consistent with the standards and criteria of U.S. postal law.

According to estimates developed by Jim Campbell, a leading consultant in this area and member of the Hudson Commission, using plausible estimates regarding the development of international postal services in the future, the terminal dues provisions in the 2016 UPU Convention would likely:

- Reduce the Postal Service’s pricing preference for delivery of Chinese e-commerce packages (i.e., the discount compared to similar domestic U.S. rates) from approximately 65 percent to 50-55 percent by 2021.
- Continue the Postal Service’s 50-55 percent discounts for delivery of e-commerce packages from industrialized countries, including Japan and Germany.

It appears, however, that this slight reduction in pricing preference for Chinese and other e-commerce businesses will be more than offset by the continuing rise in e-commerce imports, particularly from China. The total amount of discounts given to foreign e-commerce postal packages is thus likely to increase substantially.<sup>78</sup>

Moreover, it appears that the losses on the delivery of inbound international letter post will more than offset any benefits the Postal Service might reap from underpriced terminal dues for outbound mail. According to Campbell’s model, the Postal Service could suffer a negative net financial transfer of about \$1 billion over the four years from 2018-2021. In a recent, unrelated paper, the authors of the Copenhagen Economic studies for the PRC estimate that the Postal Service will experience a net financial transfer of \$233 million (SDR 170 million) in 2018 alone.<sup>79</sup>

Although the 2016 UPU Convention makes no changes in the customs and security provisions of the UPU, in fall 2016 members in both houses of Congress introduced bills

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<sup>78</sup> See estimates by James I. Campbell Jr., <http://www.jcampbell.com/UPU-TDs/TDM.html>.

<sup>79</sup> Okholm, Henrik Ballebye, Bruno Basalisco, Jimmy Gärdebrink, and Anna Möller Boivie. “Forecast e-commerce impact on international subsidies from Terminal Dues.”

that would override the Convention and require packages (“non-letter class mail”) imported via the international postal system to meet the same customs and security requirements as applied to packages by private carriers. The lead author of the “Synthetics Trafficking and Overdose Prevention Act of 2016” or the “STOP Act” is Senator Rob Portman of Ohio.<sup>80</sup> In informal comments on the Portman bill, the Department of Homeland Security repeatedly argued it may be inconsistent with U.S. obligations under the Universal Postal Convention. It appears likely these bills will be taken up in the next session of Congress beginning in January 2017.

In sum, the 2016 UPU Convention obliges the United States to comply with the main provisions of the current Convention until the end of 2021, including submission to Regulations adopted by the UPU Postal Operations Council.

Under the Convention and other acts of the UPU, the United States has only two options to mitigate some of the adverse effects of the UPU Convention described above:

- The U.S. and other like-minded countries can agree to a multilateral terminal dues agreement in which the charges for delivery of inbound international mail are properly aligned with equivalent domestic postage.<sup>81</sup>
- The U.S. and other like-minded countries can establish a Restricted Union or Special Agreement in which both the charges for delivery of inbound international mail are properly aligned with equivalent domestic postage and each country has the right to apply customs and security laws in the same manner to international documents and packages, whether conveyed by postal or private carriers. However, the legal flexibility to deviate from the UPU Convention and Regulations in such an arrangement is unclear.<sup>82</sup>

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<sup>80</sup> See S. 3292, 114th Cong., 2d Sess. (introduced, Sep 7, 2016, by Senators Portman, Johnson, and Ayotte) and H.R. 6045, 114th Cong., 2d Sess. (introduced, Sep 15, 2016, by Mr. Tiberi, Mr. Neal, Mr. Boustany, Mr. Larson of Connecticut, Mr. Chabot, Mr. Mccaul, Mr. Marchant, and Mr. Rothfus).

<sup>81</sup> UPU, 2016 Istanbul Congress, Draft Acts Doc 4, [2016] Universal Postal Convention, art. 27 (“Any designated operator may, by bilateral or multilateral agreement, apply other payment systems for the settlement of terminal dues accounts”).

<sup>82</sup> UPU, 2016 Constitution, art. 8(1) (“Member countries, or their designated operators if the legislation of those member countries so permits, may establish Restricted Unions and make Special Agreements concerning the international postal service, provided always that they do not introduce provisions less favourable to the public than those provided for by the Acts to which the member countries concerned are parties”). In 2014, the UPU’s International Bureau adopted a legal analysis that concluded postal services provided in accordance with various types of multilateral agreements may not “deviate from other consequential obligations as decided by the bodies of the UPU.” See CA C 1 RIPG 2015.1 Doc 6 and attachments. This position generated substantial controversy but no resolution prior to the Istanbul Congress.

In both cases, these reforms would apply only to postal items exchanged between the U.S. and like-minded countries, not to postal items received from the rest of the world.

Alternatively, the United States can enact legislation that overrides the 2016 UPU Convention as matter of U.S. law. A new U.S. statute would be binding on the Postal Service and the Executive Departments. However, as a matter of international law, such a step may place the United States in breach of its commitments under the acts of the UPU.<sup>83</sup> Under the UPU Constitution, the Convention and Regulations are binding on all member countries. To avoid such a breach, the United States would first have to give one year's notice to other UPU member countries of its intention to withdraw from the UPU before enacting contrary legislation.<sup>84</sup> On the other hand, the practical consequences of breaking the 2016 UPU Convention are considered minimal. The likelihood that other Posts would refuse to deliver mail from the United States or send their international mail to the United States is low. The exchange of mail between Posts is in their mutual commercial interest.

Still another option is for the United States to consider withdrawing from the UPU Convention altogether. Such a move would require taking an additional step involving Congress, which the Commission has included in its policy recommendations listed below.

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<sup>83</sup> International law is murky. However, it seems that, as a matter of international law, the State Department's conclusion of the 2016 UPU Convention is binding on the United States regardless of whether or not the State Department's actions were consistent with terms of current U.S. law and regardless of whether Congress subsequently adopts legislation overriding provisions of the Convention. See American Law Institute, *Rest. 3d. Restatement of the Foreign Relations Law of the United States* §§ 115, 311 (1987).

<sup>84</sup> UPU, 2016 Constitution, arts. 12 (withdrawal from the UPU), 22 (acts of the UPU are binding).

## ***The Way Forward***

**A**fter completing our meetings, the members of the Hudson Postal Commission agreed that our final report should include an analysis of the problems posed by the current UPU Convention, as well as other extrinsic factors, that have led to a growing “crisis in the mails.”

We include a series of policy recommendations, concrete steps that Congress and a new administration can take and/or initiate, both unilaterally and in conjunction with other leading governments, to correct many of the problems posed by the current status quo, in both the economic and the national security spheres.

### **Limit the Department of State’s negotiating mandate and authority to be consistent with U.S. law as well as competition, trade, and national security policies.**

Experience over the last several decades has amply demonstrated that incorrectly establishing rates and operational details via intergovernmental agreement that affect the exchange of international postal items causes large economic distortions. Congress should limit the scope of the State Department’s negotiating authority to agreements that are consistent with Section 407(a) of Title 39, U.S. Code, and in a manner consistent with U.S. competition, trade, and national security policies. In particular, the Department of State should not be able to establish rates or other operations standards on behalf of the Postal Service by intergovernmental agreement (any more than it should be negotiating an aviation agreement establishing the business arrangements for a specific airline). Nor should the State Department be authorized to negotiate exceptions to the customs and security laws of the United States. Customs and security agreements relating to international postal shipments, as for all other international shipments, should be developed by the Department of Homeland Security in cooperation with the World Customs Organization. Intergovernmental postal agreements should be limited to agreements that affect U.S. providers of postal and other delivery services in a competitively neutral manner.

### **Clarify the application of antitrust policy and trade law to international postal services.**

Congress should require the State Department to receive sign-off from the Antitrust Division of the Department of Justice stating that any UPU proposal doesn’t raise anti-competitive concerns or provides a distortion to competition between Postal services and private carriers. Similarly, the Department of Commerce and the Office of the U.S. Trade Representative should similarly certify to the State Department that any UPU proposal is consistent with U.S. trade policy and trade commitments.

Several studies over the last three decades point to potential inconsistencies between UPU provisions (and other inter-postal agreements), and (1) the spirit of antitrust laws of the U.S. and other industrialized countries and (2) the General Agreement on Trade in Services.

**Appoint a high-level commission to review U.S. participation in the UPU and make recommendations for steps needed to advance the national interest.**

Congress should consider appointing a high-level commission to review and reconsider the United States participation in the UPU. Although reasonable persons can disagree about the magnitude of the issues posed, the competitive inequities, economic distortions, adverse financial effects for the Postal Service, and significant risks to the security, health, and revenue of the United States summarized in this report are not in doubt. Also beyond reasonable argument is the fundamental inappropriateness of subjecting the U.S. government to binding international Regulations enacted by the UPU Postal Operations Council, a committee of foreign postal officials (with the exception of the Postal Service delegate). Nor is it reasonable that the United States needs the agreement of the UPU to take a reservation to a UPU provision that is inconsistent with the laws and policies of the United States.

The world of international communications and commerce has changed fundamentally in the last few decades. The international postal system is well along in a transition from a network of government postal administrations whose primary purpose to facilitate the exchange of letters and printed matter between nations to an association of corporatized and privatized successor businesses. Those businesses are vying to capture e-commerce packages in competition with private sector companies and, increasingly, with each other. Moreover, the development of mature global aviation and electronic communications networks —supported by data-processing capabilities unimaginable two or three decades ago — has radically changed the operational problem that the UPU was established to address. That original problem was the movement of a relatively small number of mail bags between approximately 200 national offices.

In short, the time has come to reconsider the UPU and U.S. participation in it.

At the same time, the United States can, and should, support the high social purposes for which the UPU was originally created. In the words of the Postal Accountability and Enhancement Act (PAEA), *“to promote and encourage communications between peoples by efficient operation of international postal services and other international delivery services for cultural, social, and economic purposes.”*

Likewise, the United States can and should assist citizens in needy developing countries to sustain basic cultural, social, and economic communications with other nations of the world. Yet it is reasonable to ask whether the UPU as currently organized is an appropriate vehicle for accomplishing these noble ends in the twenty-first century.

**Create an inter-agency task force to negotiate an agreement among industrialized countries establishing non-discriminatory principles for terminal dues and other charges for the delivery of inbound international mail with a target date of January 1, 2018.**

While considering whether to remain in the UPU under present rules, Congress should also create a task force composed of representatives of, at least, the Department of State, the Department of Commerce, the Department of Justice, and Office of the U.S. Trade Representative, to negotiate new terminal dues agreements among industrialized countries. The 2016 UPU Convention permits such alternative arrangements.

The new agreement should be based on the principle that, in respect to exchanges of mail between parties to the agreement, each national Post will charge the same rates for the same services regardless of the nationality or residence of the sender. Put simply, there is no reason why the Postal Service should charge a citizen of Germany or Canada or Japan more or less than an American for the same delivery service. The agreement should also provide that the national regulator in each country will protect the rights of foreign mailers in the same manner as it protects the rights of its own citizens. Each Post Office should be allowed to the same commercial flexibility in international commercial relations as it has in domestic commercial relations, but no Post should discriminate based on nationality.

Such an agreement is politically feasible. The laws of (almost) all industrialized countries reflect a reasonably similar approach to the governance of international postal services. There is no justification for perpetuation of rate discrimination among industrialized countries based on the nationality of the sender.

Although an agreement among industrialized countries will not eliminate losses on the delivery of e-commerce packages from Asia, it will eliminate the majority of other distortions created by the 2016 UPU terminal dues system. It will also substantially enhance the possibility of successful collective action to eliminate discounts for postal e-commerce imports from Asia beginning in 2022, if not before.

**Initiate a study at the World Customs Organization to harmonize rules for customs and security controls that could be applied to all low-value packages.**

Another important step in reforming the international postal package system is for U.S. Customs and Border Protection to join forces with the countries that make up the World Customs Organization (WCO). The goal is to craft a standard simplified customs form with uniform customs rules that apply to all inbound international low-value parcels and packages whether conveyed by Posts or private carriers. Such a system necessarily relies on the transmission of electronic data in advance of the arrival of packages in the port of entry. As Brenda Smith of CBP testified before our commission, for postal packages, the vast majority of its customs information still comes from paper forms, as opposed to electronic form. Switching to electronic data collection not only helps to standardize the process of gathering customs data, but also speeds the dissemination of that data. It also enables CBP to act more quickly in advance of suspicious or dangerous packages from foreign destinations.

Moreover, the growing volume of e-commerce packages and e-commerce players implies that electronic data is the best way to stay ahead of an increasingly complex game.

**Increase Postal Regulatory Commission oversight.**

The PRC can have an important role in providing active oversight of the consistency of UPU rules and regulations with U.S. law. It can also ensure that the Postal Service provide more timely, accurate, and transparent data on its international postal package business, including outbound business.

**Apply U.S. customs and security laws and regulations in the same manner to postal shipments and non-postal shipments, while allowing a reasonable transition period for foreign Posts in developing countries.**

Congress should ensure that U.S. customs and security laws, and all other laws that regulate imports and exports, are applied the same manner to postal shipments and non-postal shipments. Indeed, in the 2006 PAEA, Congress adopted a statutory mandate to this effect for all “competitive products” (as defined by the Postal Regulatory Commission) conveyed by the Postal Service and private carriers. 39 U.S.C. § 407(e)(2). This statute, however, has remained without effect for ten years. It is apparent that further, more explicit legislation is needed to protect the security, health, and revenue of the United States.

Congress should also extend the scope of non-discriminatory treatment to include all postal shipments, not only “competitive products.” For inbound shipments, transportation services for all types of documents and packages are competitive up to the port of entry. In almost all countries, Posts and private carriers compete in the “upstream” portion of the international market, i.e., in the collection and transportation of bulk shipments. In the United States, this is also true even though the Postal Service may be the market dominant supplier of delivery services (as in the case of letters). It may be reasonable (as the UPU maintains) for U.S. customs and security regulations to apply differently to documents and goods. There is, however, no apparent reason why the regulations should apply differently to documents or goods based on the *identity* of the carrier.

At the same time, however, the Commission recognizes that the UPU’s concerns on this issue are legitimate. CBP should be given reasonable flexibility to adjust the application of customs and security regulations to take into account the technical capabilities of Posts in developing countries, especially regarding non-commercial mail. On the one hand, CBP should not place demands on foreign Posts that unreasonably impede the flow of mail.

On the other hand, CBP should not risk the security or health of Americans simply to accommodate a foreign Post that is reluctant to invest in necessary operational

*Arthur Herman*

improvements. CBP, working in coordination with the World Customs Organization, should have the discretion to strike an appropriate balance.

### ***The Hudson Institute Postal Commission***

The Hudson Institute Postal Commission convened on September 15 and September 16, 2016 to analyze the impact of the Universal Postal Union's (UPU) international package shipment regulations on the United States and to compose a series of recommendations. The group of seven commissioners heard testimony from experts in the fields of national security, customs and border protection, e-commerce, and international shipping. The Commission ultimately located key areas of concern as a result of UPU regulations, which included disadvantaging the competitiveness of U.S. merchants, facilitating the shipment of illicit drugs into the U.S., increasing threats to national security, and imposing costs on the United States Postal Service and U.S. Customs and Border Protection. The Commission's recommendations outline steps for mitigating the negative effects imposed by current UPU regulations.

Dr. Arthur Herman would like to thank the commissioners for their help with the research and writing for this report.

#### **Commission Members:**

**Dr. Arthur Herman (Chair)** is a Senior Fellow at Hudson Institute. He is the author of seven books, including the *New York Times* bestselling *How the Scots Invented the Modern World* (2001); the Pulitzer Prize Finalist *Gandhi and Churchill* (2008); *To Rule the Waves: How the British Navy Shaped the Modern World* (nominated for the UK's Mountbatten Prize); and the highly acclaimed *Freedom's Forge: How American Business Produced Victory in World War II*, which *The Economist* magazine picked as one of the Best Books of 2012. His most recent work, *Douglas MacArthur: American Warrior*, was published by Random House in June of 2016. His previous book, *The Cave and the Light: Plato Versus Aristotle and the Struggle for the Soul of Western Civilization*, was published by Random House in 2013. Educated at the University of Minnesota and Johns Hopkins University in history and classics (Ph.D. 1985), Dr. Herman is a frequent contributor on defense, energy, and technology issues to *Commentary* magazine, the *New York Post*, *National Review*, and the *Wall Street Journal*. He was also the first non-British citizen to be named to the Scottish Arts Council from 2007 to 2009. His newest book *1917: Woodrow Wilson, Vladimir Lenin, and the Year That Created the Global Future* will be published by Harper Collins in 2017.

**Jim I. Campbell** is a lawyer and consultant in Washington, D.C. He is a long-time adviser to Federal Express Corporation on U.S. postal reform and international postal policy. In addition, in recent years he has co-authored, with the German Wissenschaftliches Institute für Kommunikationsdienste, several major studies of European and international postal laws and practices for the European Commission and a review of the history and development of postal law and the postal monopoly in the United States for the Postal Regulatory Commission. Jim Campbell began his career as a staff attorney for the Subcommittee on Administrative Practice and Procedure of United States Senate. In 1976 he joined DHL and led efforts to reform national and

international postal, customs, and aviation regulations that impeded the development of the then fledgling international express industry. Jim Campbell was born in Baltimore, Maryland. He graduated from Princeton University and Georgetown University Law Center. He is the author of many articles on postal policy and a book on postal policy and the express industry.

**Dr. R. Richard Geddes** is a Professor in the Department of Policy Analysis and Management at Cornell University and Director of the Cornell Program in Infrastructure Policy. Geddes is also a core faculty member of the Cornell Institute for Public Affairs (CIPA) and a Visiting Scholar at the American Enterprise Institute (AEI). He is a Research Fellow with the Mineta Transportation Institute at San Jose State University. Geddes was also a Fulbright Senior Scholar during the 2009-2010 academic year to study transportation public-private partnerships in Australia, and a Visiting Faculty Fellow at Yale Law School during the 1995-1996 academic year. He has advised numerous Fortune 500 companies, including United Parcel Service and CSX. Geddes' publications have appeared in numerous academic journals, including the *American Economic Review*, *Journal of Regulatory Economics*, *Journal of Legal Studies*, *Journal of Law & Economics*, *Transportation Research Part A*, and *Journal of Law, Economics, and Organization*, among others. Geddes holds MA and Ph.D. degrees in economics from the University of Chicago, and a BS in economics and finance from Towson State University.

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**John Horton** is the President and CEO of LegitScript. John sets LegitScript's overall strategy and oversees its execution. He founded LegitScript in 2007, after working for five years as a drug policy advisor in the White House, where he helped the Drug Czar coordinate national policy on prescription drug abuse, methamphetamine and chemical diversion. He previously worked as a prosecutor and legal counsel to the Oregon House Judiciary Committee. John lived for several years in Tokyo, where he worked in the finance industry and pursued a Master's degree in International Law.

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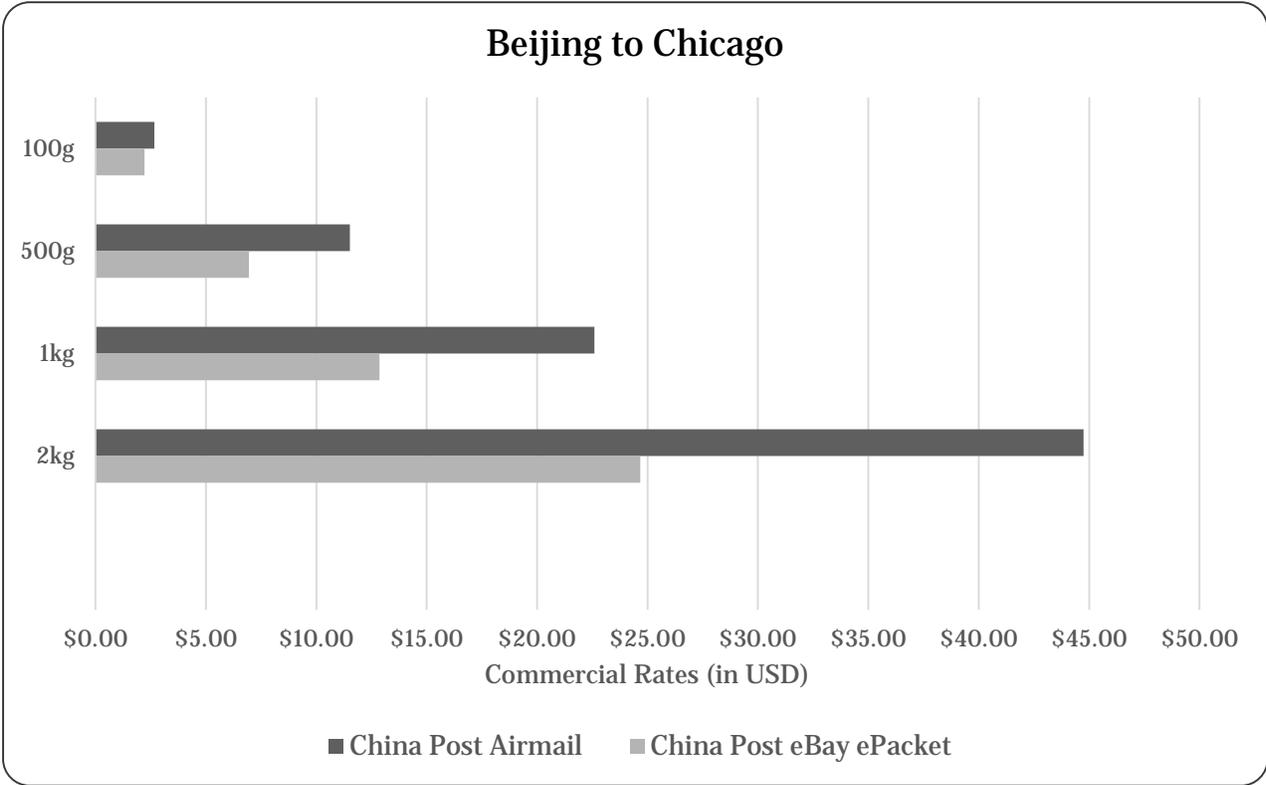
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Appendix<sup>85</sup>

Cost to ship to Chicago from Beijing<sup>86, 87</sup>

Beijing to Chicago				
	100g	500g	1kg	2kg
China Post Airmail	\$2.66	\$11.52	\$22.60	\$44.75
China Post eBay ePacket	\$2.22	\$6.95	\$12.86	\$24.68



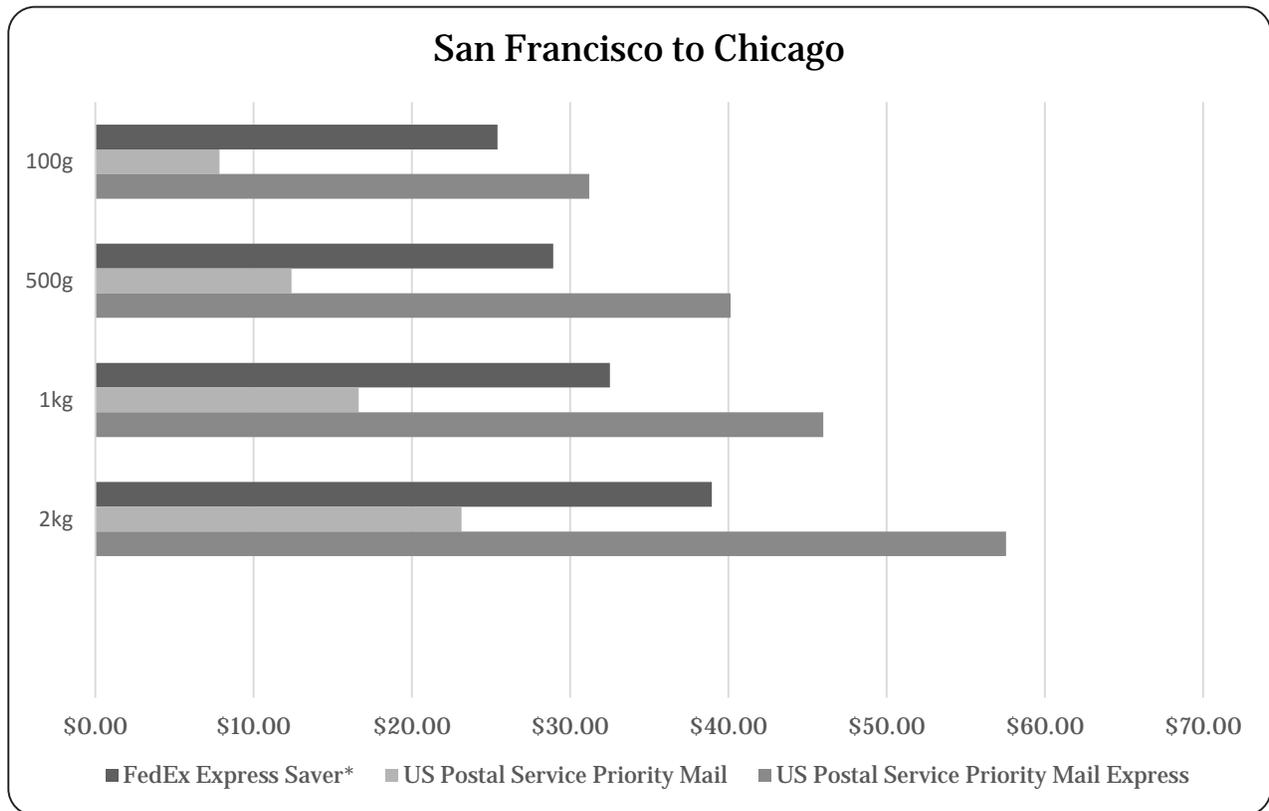
<sup>85</sup> Compiled by Ivan Teo, November 2016

<sup>86</sup> <http://zf.chinapost.com.cn/index.do>

<sup>87</sup> <http://www.chinapostaltracking.com/ems/ebay-epacket-eub/>

**Cost to ship to Chicago from San Francisco** <sup>88, 89</sup>

<b>San Francisco to Chicago</b>				
	<b>100g</b>	<b>500g</b>	<b>1kg</b>	<b>2kg</b>
<b>FedEx Express Saver</b>	\$25.41	\$28.94	\$32.52	\$38.96
<b>US Postal Service Priority Mail</b>	\$7.85	\$12.40	\$16.65	\$23.15
<b>US Postal Service Priority Mail Express</b>	\$31.20	\$40.15	\$46.00	\$57.55



<sup>88</sup> <https://www.fedex.com/ratefinder/home?cc=US&language=en&locId=express>

<sup>89</sup> <https://postcalc.usps.com/Default.aspx?m=0&dpb=0>

***List of Names and Acronyms***

Universal Postal Union	UPU
Postal Regulatory Commission	PRC
Postal Accountability and Enhancement Act	PAEA
United States Postal Service	USPS
Extraterritorial Offices of Exchange	ETOE
Automated Manifest System	AMS
Customs and Border Protection	CBP
Air Cargo Advance Screening	ACAS
Postal Operations Council	POC
European Union	EU
Express Mail Service	EMS
World Customs Organization	WCO
Cornell Institute for Public Affairs	CIPA
American Enterprise Institute	AEI
Global Regulatory Cooperation	GRC
Office of National Drug Control Policy	ONDCP

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