Post Sector Report

1. This is a report for the House of Commons Committee on Exiting the European Union following the motion passed at the Opposition Day debate on 1 November, which called on the Government to provide the Committee with impact assessments arising from the sectoral analysis it has conducted with regards to the list of 58 sectors referred to in the answer of 26 June 2017 to Question 239.

2. As the Government has already made clear, it is not the case that 58 sectoral impact assessments exist. The Government’s sectoral analysis is a wide mix of qualitative and quantitative analysis contained in a range of documents developed at different times since the referendum. This report brings together information about the sector in a way that is accessible and informative. Some reports aggregate some sectors in order to either avoid repetition of information or because of the strong interlinkages between some of these sectors.

3. This report covers: a description of the sector, the current EU regulatory regime, existing frameworks for how trade is facilitated between countries in this sector, and sector views. It does not contain commercially-, market- or negotiation-sensitive information.

Description of sector

Key statistics

- GVA (Gross Value Added) was £12 billion in 2015, or 0.7 per cent of total UK GVA;

- The postal services sector provides a key component of the UK’s infrastructure that underpins other sectors. Financial services (£10 billion per annum), retail/wholesale (£2.3 billion per annum) and the Government (£1.5 billion per annum) are large users of postal services;

- The sector accounts for 399,000 jobs, or 0.9 per cent of the UK workforce; and

- 91 per cent of those employed are UK nationals; 5 per cent are non-UK EFTA nationals

Detail

4. Postal services are visible and valued by both members of the public and businesses. The postal service is an enabler of trade: companies of all sizes use it to build their business, supply goods and receive payment. It is also used by all levels of Government for all public communications and is important for vulnerable consumers who rely on the services it provides. The sector helps maintain and create
infrastructures to support trade and, for e-retailers, the sector’s performance is key to delivering a quality service to their customers.

5. Royal Mail (RM) is the incumbent network operator and the designated UK Universal Service Provider (USP) delivering the UK universal service – the “one price goes anywhere 6 days a week” letter service. It has around 142,000 frontline employees, 115,000 pillar boxes, 8 regional distribution centres, 39 mail centres and around 1,400 local delivery offices.\(^1\) It has a road fleet of more than 40,000 vehicles and access to rail and air transport networks. Parcelforce Worldwide operates a separate UK network for express parcels. In 2016-17, Parcelforce Worldwide processed around 96 million parcels. Royal Mail’s national postal network is included in the Government’s Critical National Infrastructure framework, as a sub-sector of the Communications sector.

6. Public access to RM’s Universal Service Obligation (USO) is principally through the 11,600 post office branches operated by Post Office Limited (POL). POL provides access to its network and acts as an agent for Royal Mail for mail services under a commercial agreement between the two parties. This network makes POL one of the largest retailers in the UK. More than 17 million customers, including c.30 per cent of UK small businesses, visit a branch each week. POL separated from RM in April 2012 and it now operates as an independently managed and governed business. POL is wholly Government owned.

7. In 2015-16 POL’s pre-subsidy revenue of £870 million was made up of Mail and Retail (c.43 per cent), Financial Services (a mix of personal and business banking services, insurance and foreign exchange c.34 per cent), Government Services (c.11 per cent) and Telephony and Other (c.11 per cent). With this range of services, POL, as an agent of RM, complies as required with RM’s postal regulation requirements (particularly VAT and USO requirements), financial services and telecoms regulation. POL has an interest in the payments, travel, personal financial services and insurance markets.

8. POL is subsidised by the Government to maintain a network above an optimally commercial size to provide access to key services of general economic interest, which it offers in line with national access criteria for post office coverage (such as pensions and benefits payments, access to cash and basic banking facilities, mail services and payments). The Government also provides investment funding to modernise and transform POL’s network to make it more efficient and sustainable in the long-term, and thereby less reliant on taxpayer support. Subsidy has declined from a peak of £210 million in 2012, to £70 million in 2016.

9. While post offices are a key part of the infrastructure that enables RM to meet public access to USO services, books of stamps are available more widely and RM has been growing its direct sales through the internet and offering its delivery offices as additional access points. Under the Mails Distribution Agreement put in place at the time of the separation of RM and POL, POL is unable to offer parcel services for... 

\(^1\) Royal Mail Annual Report 2016-17
other parcel operators. This effectively ties its success in the parcels environment to the performance of RM.

10. The postal market can be split into two markets: letters and parcels.

11. Within the letters market, there are two sub-markets: the access market\(^2\) (responsible for collecting and sorting mail) and delivery (end-to-end) market. The UK has the most competitive access market in Europe with access operators (i.e. not RM) accounting for 60 per cent of letter volumes in 2016.\(^3\) Access operators in Germany (which has the 2nd most competitive volumes in 2016) have only a quarter of the market share of UK access operators (as of 2013).\(^4\) There is limited competition in the UK delivery market.\(^5\)

12. Around 91 per cent of all mail originates from business. The provision of postal services to private customers is dependent on the critical mass of volume sent by large business customers and the business-to-consumer volume that they generate. Significant volume is generated by the financial services sector in the form of transactional and direct advertising mail. Other large volume businesses come from the home shopping, retail, and government sectors.

13. Consumers continue to attach relatively high levels of importance to receiving formal communications in the post. Almost eight in ten consumers (79 per cent)\(^6\) consider receiving bank statements or other financial documents in the post as very or quite important. While some recognise the ease and convenience of items such as bank statements and utility bills moving online, others value receiving paper copies for various reasons, including confidentiality.

14. The parcels market is currently largely unregulated\(^7\) at EU and UK level. It is highly competitive, particularly for heavier parcels and for bulk parcel contracts. In parcels, approximately 12 parcel delivery companies operate nationally alongside hundreds of smaller local operators. There is significant investment in additional capacity to keep up with the rapid growth in e-commerce – the Office for National Statistics (ONS) estimated that online sales grew by 21 per cent in 2016 alone.\(^9\)

15. The parcel delivery market is more competitive than the letter delivery market and Ofcom have identified 13 major operators that compete with Royal Mail in parcel delivery.

16. The express industry specialises in time definite, reliable and efficient transportation, on a door-to-door basis. A large proportion of shipments carried are high added

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\(^2\) Access refers to customers and competitors using third-party access to Royal Mail’s delivery network.
\(^3\) Downstream access agreements allow alternative operators to collect and sort customers’ mail into Royal Mail’s inward mail centres, turning it over to Royal Mail for delivery.
\(^4\) Response to Ofcom’s May 2016 Fundamental Review of the Regulation of Royal Mail, Royal Mail
\(^5\) Ofcom report ‘Review of the Regulation of Royal Mail’, 25 May 2016
\(^6\) Citizen’s Advice, ‘The Future of Consumer Needs for Postal Services’, August 2016
\(^7\) Single piece parcels up to 20kgs are included in EU minimum universal service requirements.
\(^8\) The Commission published a draft Regulation on cross-border parcel delivery in May 2016
\(^9\) ONS Retail Sale Index – Internet Sales
value, for example electrical and engineering components. Express shipments generally have to reach market quickly, for example pharmaceutical items for clinical trials, spare parts and contract documents. The customer is provided with shipment status information, through track and trace, throughout the delivery process with deadlines for deliveries in many instances guaranteed. A growing proportion of express services are e-commerce business to consumer (B2C) traffic but consumer to consumer (C2C) traffic is negligible.

Market shares (revenues) for UK parcel delivery

![Market share chart](chart.png)

Source: Royal Mail half year 2016-17 Results. Note: Parcelforce is part of Royal Mail Group

Cross-border postal items

17. In 2013 around 4.4 per cent of all RM letter volumes were international (around 734 million letters).\(^\text{11}\) Around 360 million parcels were exported to, or imported from, the UK in 2015-16,\(^\text{12}\) accounting for 18 per cent of all UK parcel volumes. UK cross-border/international parcels account for 19 per cent of RM's UK Parcels, International and Letters\(^\text{13}\) (UKPIL) parcel volumes and 18 per cent of its revenue (as of 2015/16).

18. The EU is the UK’s largest e-commerce trading partner. MetaPack report that over half of the parcels exported from the UK go to the EU.\(^\text{14}\) This is consistent with data from Volo that indicates that France and Germany constitute 40 per cent of exports for UK-based online retail Small and Medium Enterprises (SMEs).

19. The EU is also thought to be the largest market for UK consumers buying online. An EU study estimates that 83 per cent of UK e-commerce spending goes to UK retailers, followed by 12 per cent to EU retailers and six per cent to non-EU retailers (2014).\(^\text{15}\) Additional measures under the EU’s 2015 Digital Single Market package

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\(^{10}\) Royal Mail half year 2016-17 Results. Note: Parcelforce is part of Royal Mail Group

\(^{11}\) Universal Postal Union

\(^{12}\) Annual Monitoring Update Report on the Postal Market 2015-16, Ofcom

\(^{13}\) UKPIL is the RM network that provides the universal postal service, including letter and parcel services to and from countries around the world


\(^{15}\) Consumer Perceptions of (Cross-border) e-commerce in the EU Digital Single Market, European Commission, 2015
are aimed at increasing cross-border e-commerce in the future. Under current operating frameworks, RM expects parcel deliveries to the EU to grow.

**Border Processes**

20. RM is the only universal service provider in the UK and, as such, is the only operator in the UK permitted to use the simplified postal customs clearance procedures set down by the Universal Postal Union, the United Nations (UN) intergovernmental organisation for postal services, and in the Union Customs Code (UCC - the EU law underpinning customs control across the Customs Union). Under the UCC, goods and gifts with a value of up to €1000 arriving from outside the EU can be customs cleared using form CN22/23, usually completed by the sender of the parcel. Items with a value of €1000 or above require a full customs declaration.

21. For third country imports and exports, the goods must be cleared at RM’s Offices of Exchange (OoE) at Coventry for parcels and Heathrow for small packets up to 2kg. Border Force (BF) staff are permanently deployed at these sites to carry out customs safety and security checks and fiscal controls. The burden is greater at import rather than export because there are no tariffs imposed on exports. At import, as well as safety and security checks, Her Majesty’s Government (HMG) also has to consider if there is a tax liability and if so raise a charge. For current third country traffic, HMG raises approximately 1.2-1.5 million charges per year. This is only a small proportion of the traffic because the postal international supply chain is mostly used for low value goods that have an exemption from customs charges. The current UK threshold is set at £15, except for the Channel Islands which is set at £0 for competition reasons. The charges are paid by operators and then recovered from the consumer at the doorstep.

22. Unlike goods imported as cargo, including by the express industry operators, postal is currently exempt from providing safety and security declarations to customs. This exemption ceases in 2020. The Universal Postal Union (UPU) Customs Declaration Service IT system will transform a largely manual customs presentation process to an e-enabled system, using data sent electronically from the sending country. This system is being rolled out iteratively and should be fully deployed by 2019. However, there will be some sending countries that cannot provide this data electronically and a manual fallback system will be required.

23. HMRC is the UK customs authority and has responsibility for policy for goods imported and exported via post.

**Trends**

24. The letters market is declining, driven by e-substitution away from letters towards digital forms of communication, whereas the parcels market is growing, driven by online retail. Parcels now account for 44 per cent of Royal Mail UK. The chart below illustrates this.

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16 Royal Mail Annual Report 2016-17
25. There continue to be developments in international B2C delivery markets that will provide significant challenge to traditional delivery companies. For example, Amazon has shifted from postal customer to competitor by starting its own delivery services.

The current EU regulatory regime

Summary

26. EU Postal Services legislation stipulates that basic postal user needs are met under a Universal Service Obligation (USO) which sets minimum standards to be guaranteed by Member States and more widely across the sector. The Postal Services Act 2011 sets minimum requirements for the UK postal service, which can only be changed by Parliament. The Office of Communications (Ofcom) sets the specification of the postal service in the UK. The UK’s universal postal service goes beyond that set under EU law.

27. Ofcom is the regulator of the postal services sector. Ofcom’s primary duty is to maintain a financially sustainable and efficient universal postal service. Subject to this, Ofcom is also required to ensure that the postal services market is working in the interests of consumers, for example by promoting competition. Ofcom has set a price cap on Royal Mail’s 2nd class letters and parcels; regulates access to the RM delivery network to facilitate access competition; and monitors the financial sustainability and efficiency of the universal postal service. Ofcom’s duties and powers are set out in the Postal Services Act 2011, which transposes the Postal Services Directive (2008/6/EC).

28. UK legislation allows for the protection of the minimum requirements of the universal postal service. These can only be changed with the approval of Parliament.

EU framework for letters and parcels

29. EU policy aims to reconcile the interests of a number of key stakeholders, such as national postal operators (universal service providers (USP)), other postal operators (including express operators), new entrants to the postal market and
users/consumers, while also striking the right balance between increasing competition and the sustainable maintenance of the universal service. There have been three Postal Directives, implemented to address sectoral challenges relating to underlying structural problems and wide divergences between Member States. The Directives define the minimum requirements of the universal postal service to be guaranteed by each EU country and fully open the sector to competition.

30. The First Postal Services Directive (PSD) 97/67 EC established a regulatory framework for European postal services. It was adopted in 1997 and aimed to improve domestic and intra-EU postal services by addressing the low quality of service and efficiency; the lack of customer focus, choice and innovation; limited cooperation between operators; and ongoing state subsidies. The Postal Services Directive requires the use of European technical standards in some cases. EU countries are required to ensure that the quality of service is measured under standardised conditions, for example standard delivery times for letters and parcels arriving from EU countries.

31. Among the key elements of the First Postal Services Directive were the establishment of a universal service, with minimum scope, frequency and quality of service requirements, a number of tariff principles and the creation of independent national regulatory authorities (NRAs) for postal services. An essential element of the modernisation strategy was the ‘gradual and controlled liberalisation of the market’.

32. In 2002, as a further step in that direction, the Second Postal Services Directive, among other amendments, reduced the price and weight limits for the reserved area, thus reducing the scope of the monopoly of the national postal operators.

33. In February 2008 the Third Postal Services Directive (PSD) set the timetable for full market opening and included strengthening the tasks and competences of NRAs; changes in the manner in which the universal service could be provided and financed; requiring certain elements of the postal infrastructure (such as address databases and letter boxes) to be accessible to multiple operators; strengthening and broadening the legal requirements for information and data collection by NRAs; and extending consumer protection provisions.

34. The Commission noted, in its 5th Application Report, published in November 2015 that the number of Member States that exceed the minimum (five day) provision of collection and delivery days was declining. Many of the responses to its autumn 2014 consultation on this issue called for a reduction in the scope of the USO, at least at EU level, to give MSs greater flexibility, given the declining nature of domestic letter markets.

35. The UK was one of the first Member States to fully liberalise its postal market (January 2006), well in advance of the December 2010 deadline. The UK transposed the Directives under the Postal Services Acts 2000 and 2011. UK legislation goes beyond the EU minimum e.g. it requires Royal Mail to deliver letters 6 days per week, instead of 5, at a uniform price across the whole country. The following table highlights the minimum universal service requirements at EU and UK levels.
EU & UK minimum requirements for the universal postal service:

<table>
<thead>
<tr>
<th>EU: Postal Services Directive(s) (covers national and cross-border services)</th>
<th>UK: Postal Services Act 2011</th>
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<tbody>
<tr>
<td>Permanent provision of specified quality (quality standards set by Ofcom in the UPSO).</td>
<td>Six day a week letters delivery and collection service to every address in the UK</td>
</tr>
<tr>
<td>Collection and delivery every working day and not less than five days a week</td>
<td>Five day a week parcels (up to 20kg) delivery and collection service to every address in the UK</td>
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<tr>
<td>Postal items up to 20kg</td>
<td>Postal services at an affordable, uniform tariff across the UK</td>
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<tr>
<td>Minimum and maximum dimensions for postal items meet UPU provisions.</td>
<td>A free-of-charge postal service to blind or partially sighted people</td>
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<td></td>
<td>A registered items and insured items service at affordable prices</td>
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<td></td>
<td>Free carriage of legislative petitions and addresses</td>
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36. The UK Postal Services Act 2011 transferred the regulatory function of the postal sector to Ofcom. It set up a new regulatory framework in 2012, which gave RM greater commercial freedom to compete by removing most of its revenues under direct price regulation (from 80 per cent to less than 10 per cent). It retained a price cap on 2nd class letters and parcels under 2kg to protect vulnerable consumers and ensure a basic universal service was available to all. Under the Directives, Member States retain significant freedoms to set their national postal services requirements.

37. Overall, the cumulative effect of the UK legal and regulatory framework is that the universal service obligation extends beyond that set out under EU law.

Parcels

38. The UK parcel market is largely unregulated. The EU Postal Services Directive and the UK’s universal service obligation include single piece parcels up to 20kg in the minimum universal service requirements.

39. In May 2016, the Commission adopted a proposal for regulation on cross-border parcel delivery (COM(2016) 285 final) as part of its Digital Single Market (DSM) Strategy. The aim of the proposal is to address specific issues relating to cross-border parcel delivery services by: making the market work more effectively, improving regulatory oversight of the market, encouraging competition, increasing the transparency of tariffs in order to reduce price differentials and lower the prices paid by individuals and small business, especially those in remote areas. The Presidency aims to conclude the negotiations in December 2017.
Cross-sectoral rules

40. The VAT Directive exempts public postal services supplied by RM under a universal service obligation from VAT. It has been recognised that the VAT exemption could have a negative impact on emerging competition in this area.\(^\text{17}\)

41. The Digital Single Market Strategy also proposes the abolition of Low Value Consignment Relief (LVCR). LVCR is an operational easement that allows customs authorities not to raise fiscal charges on consignments of low value as the cost of doing so will often outweigh the revenue benefit. In the EU, Member States can set the LVCR threshold between 10 and 20 euros. In the UK it is currently set at £15 for all countries except the Channel Islands, where it is set at £0.

42. As e-commerce thrives and end consumers increasingly buy goods online from around the world, the consequences of LVCR mean that domestic producers and retailers find it difficult to compete against cheap imports. This is having an effect across the EU. Abolition of LVCR is planned for 2021.

International Rules and Standards - UPU (Universal Postal Union)

43. The UPU has 192 member countries. It is the primary forum for cooperation between governments, designated postal operators, national regulatory authorities and many other postal-sector stakeholders. The UPU:

- Maintains a universal postal network;
- Establishes the rules for international mail exchanges among its member countries; and
- Makes recommendations to modernise products and services, stimulate mail volume growth and improve the quality of service for customers.

44. The UK is represented by Royal Mail at UPU fora – Government provides a formal mandate for it to coordinate UK interests in international postal affairs.

European Committee for Standardisation (CEN)

45. Since 1993, the European Commission has promoted and supported the process of technical standardisation in the postal sector. The Postal Directive recognises the role standardisation can play in benefitting postal customers, such as by providing a standardised measurement of quality.

46. The EU recognises the European Committee for Standardisation (CEN), one of three European Standardisation Organisations, as being responsible for developing and defining voluntary standards at European level, including for postal services. There is

\(^{17}\) Ofcom report ‘Review of the Regulation of Royal Mail’, 25 May 2016
a dedicated CEN Technical Committee (TC/331) working on this. It takes into account measures adopted at international level, and in particular those decided upon within the Universal Postal Union (UPU). UPU and CEN signed a Memorandum of Understanding in 2001 to strengthen information exchange and cooperation.

47. Postal standardisation focuses on:

- The harmonisation of technical methods at EU level within the universal postal service (in particular for external measurement of quality of service performance);
- Enabling interoperability of postal industry stakeholders; and
- Improving the effective transit of cross border parcels between national Posts (universal service providers).

**European Regulators Group for Postal Services (ERGP)**

48. The ERGP provides a consultative and advisory service to the Commission in the postal services field. It facilitates consultation, coordination and cooperation between the independent National Regulatory Authorities (NRAs) in Member States and the Commission, to ensure the consistent application of the Postal Services Directives across the EU. The ERGP plays an important role in postal reform and oversight.

**CERP (Committee of European Postal Regulators)**

49. CERP brings together representatives of ministries and regulatory authorities in postal services from 46 states. It is an important network facilitating the exchange of information and experience as the basis for the development of the regulatory role, and an essential partner for the Commission when it comes to bringing that experience to bear on international issues beyond the EU. The UK could continue to participate in discussions post EU exit.

**Devolved Administrations/Crown Dependencies and British Overseas Territories**

50. In respect of the Devolved Administrations, postal services is a reserved matter.

51. In Northern Ireland (NI), almost a quarter of businesses and one in ten consumers have taken mail across the border and posted from a post box or post office in Ireland. As cross-border e-commerce grows, consumers in NI are using a wide range of delivery solutions that are more suitable to their needs including using addresses of friends or relatives in Ireland for online deliveries.18

52. Gibraltar is a UK Overseas Territory and also a member of the European Union. It is not a member of the EU VAT area or Common Customs Territory. EU legislation in the postal sector in general applies to Gibraltar but not the Crown Dependencies or other Overseas Territories.

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18 Border Post: A report on cross border mail delivery, The Consumer Council, NI
53. The Channel Islands and the remaining British Overseas Territories are consulted on UPU international postal matters.

**Existing frameworks for how trade is facilitated between countries in this sector**

54. The arrangements described in this section are examples of existing arrangements between countries. They should not be taken to represent the options being considered by the Government for the future economic relationship between the UK and the EU. The Government has been clear that it is seeking pragmatic and innovative solutions to issues related to the future deep and special partnership that we want with the EU.

55. There are a number of existing arrangements which govern the way in which other countries trade with each other in this sector, particularly in terms of parcel delivery.

56. Postal services are included in the EU's bilateral Free Trade Agreements with third countries, focussing on minimum regulatory provisions and commitments. The requirements do not place any additional burdens on EU governments, National Regulatory Authorities or Universal Service Providers. Rather they replicate standards and minimum requirements of the existing EU legislative framework. The EU-Canada Comprehensive Economic and Trade Agreement (CETA) includes provisions for increasing the transparency of regulation, including liberalising postal services.

57. The World Trade Organisation reports that a total of 54 WTO members have commitments on courier services and/or postal services (counting the European Union as one), as of 31 January 2009. The principles of trade in postal and courier services (including express delivery) are contained, as for all services, in the General Agreement on Trade in Service (GATS).

58. In the ongoing WTO negotiations on the Trade in Services Agreement\(^1\), postal proposals have underscored the need for commitments resulting in more extensive coverage of these services in the schedules of commitments. In identifying barriers to market access and national treatment, some proposals have emphasised the existence of monopolies, while others have focused on measures discriminating against foreign suppliers. Some delegations have encouraged the undertaking of additional commitments in schedules to address certain regulatory issues. Anti-competitive practices, cross-subsidies, universal service obligations, independent regulators and licensing procedures are some of the issues mentioned in this regard. The right of members to define the kind of universal service they wish to maintain has not been questioned, as suggestions have focused on such aspects as transparent, non-discriminatory and competitively neutral implementation.

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\(^1\) The Trade in Services Agreement (TiSA) is a trade agreement currently being negotiated by 23 members of the World Trade Organization (WTO), including the EU.
59. There are also wider examples provisions for the postal sector in trade discussions. For example, on discussions on the Trade in Services Agreement (TiSA) potential arrangements consistent with the EU Postal Directive were considered. The draft Free Trade Agreement on Delivery Services provides for: i) independent regulation; discretion on the form of a universal service provider; and competition across the sector. This include a prohibition on anti-competitive behaviour by monopoly postal operators.

60. Customs arrangements are increasingly important for postal sector due to the rising demand for cross-border online purchases. The EU has customs facilitation agreements with a number of third countries, including Canada, South Korea and Switzerland. These agreements differ in the depth and scope of facilitation offered, but in summary, include:

   a. Comprehensive Economic and Trade Agreement (Canada) - provides, for example, that the parties adopt or maintain simplified customs procedures in order to facilitate trade between the Parties and reduce costs for importers and exporters. The Parties agree to applying risk assessment principles to the decision to examine goods, rather than requiring each shipment offered for entry to be examined. The EU and Canada also undertake to cooperate on interoperable systems and in international fora.

   b. EU-South Korea Free Trade Agreement - provides, for example, the advance electronic submission and processing of information before physical arrival of goods, in addition to the parties endeavouring to apply simplified procedures for economic operators.

   c. Agreement with Switzerland - provides for general cooperation and administrative assistance, mutual recognition of inspections and documents certifying compliance with the other parties’ rules, in addition to the facilitation of 24 hour crossing and express lanes. The Swiss agreement also provides for mutual recognition of Authorised Economic Operators, and facilitation in respect of security-related customs controls.

**Sector views**

[This information was provided by the Government to the Committee, but the Committee has decided not to publish this section]
Annex: Stakeholder Engagement on European Union Exit (EU Exit) in the Department for Business, Energy and Industrial Strategy

[This information was provided by the Government to the Committee, but the Committee has decided not to publish this section]