Passing the Contract Carriage Test

Shippers need to carefully analyze their transportation operations, needs before making dedicated sourcing decisions

By John A. **Gentle** and Christopher A. **Gentle**
John A. Gentle & Associates

We recently read a story about a trucking company that blamed its bank for the trouble that arose when it could not repay a loan and the bank sued.

The carrier suggested that the bank should have known better. Had it paid more attention to the trucker's financial condition it would not have loaned the carrier the money in the first place.

If you currently use or are contemplating using contract carriage and you subscribe to the philosophy that regardless of what happens, it is never your fault, then you can clearly skip this article.

If, however, you consider yourself to be well schooled and a risk manager who believes in accountability for your actions … then this article about dedicated contract carriage is for you.

It may confirm your beliefs or it may shed another view on this subject and how it can have positive or potentially devastating impact on your company and more importantly your personal career and reputation.

First, it is important to understand that for the purpose of this article we are considering the words "dedicated" and "contract carriage" to be synonymous.

In the end the shipper may either choose to:

1) Secure his own equipment and manage the transportation process;

2) Contract with others who provide the drivers and equipment and then work with them to manage the process; or

3) Outsource transportation to an asset-based logistics company and provide cursory oversight.

Only a detailed strategy with clear expectations, knowledgeable business players and a well-disciplined, interactive process will create the desired results.

Imagine you're taking an end-of-semester exam in logistics and transportation. Your professor has told you that this is going to be a blue book about dedicated contract carriage and the first question on the board is, "What are the key indicators that suggest there is an opportunity to create a contract carriage operation? And which of the key indicators have the most weight?"

If you respond that the basic drivers are capacity/volume, cost and service, that would be a very sophomoric. If you add "combining and leveraging inbound and outbound activities to improve supply chain efficiencies," that would be more in line with what logistics professionals Gary Palmer and Paul Newbourne have in mind when they think about contract or dedicated carriage.

It's not just about squeezing dollars from distribution networks, says Newbourne, vice president and general manager of Leveraged Execution Providers, a Pittsburgh-based logistics network manager focused on the food service industry.

"The underlying driver of a contracted/dedicated decision is really the perceived value from a service and cost standpoint," he says. "Sometimes dedicated operations cost more to operate but service levels improve dramatically. In other instances the results may be closer to a wash versus for-hire but the assured capacity availability and generally better service levels are worth the commitment. In the end, it's a balanced decision making process based on your customer's requirements and your tolerance for risk and/or expense"

Others suggest a key factor is whether there is a "strong potential for third-party backhaul opportunities." If you're already finding significant and consistent backhaul opportunities in the spot market, then the decision boils down to the perceived value of improved service.

Although service and efficiency are key drivers in any dedicated/contract decision, there are other qualifiers to consider, says Palmer, senior director of transportation for True Value.

Those qualifiers include the ability to obtain reliable forecasts and evaluate how demand variability might affect the operation; the ability to partition out the dedicated operation without compromising other parts of the business or its resources; the impact of the dedicated operation on price negotiations in non-dedicated lanes; and last but most critical, management's willingness to make the financial commitment.

When Palmer was asked whether it is hard to sell management on a dedicated fleet, he said that "it's not hard if it is based on a well-grounded analysis that focuses on cost savings, inventory reductions and service improvements relative to improved on-time pick-up, delivery, shorter or more consistent transit time."

We completely agree with Gary, but we also recognize that many shippers are short on logistics talent and may attempt a program without conducting the needed research. Carriers and logistics companies need to carefully scrutinize shipper information and expectations and not accept everything at face value.

The next exam question appears to be a pretty simple one — What kind of information do carriers need from shippers to understand their requirements and prepare a complete and meaningful quotation?

The Achilles' heel of any initiative, but especially for a dedicated contract carriage commitment, is the inability of some shippers to recognize the type, depth and accuracy of the needed data. Too often they don't use analytical tools or conduct the necessary in-depth analysis or engage consultants who can provide the multidimensional perspectives crucial to the development of that analysis. Although most major shippers present carriers with a strong set of requirements, the real world of shipping and receiving often differs from the written word. Carriers bid based

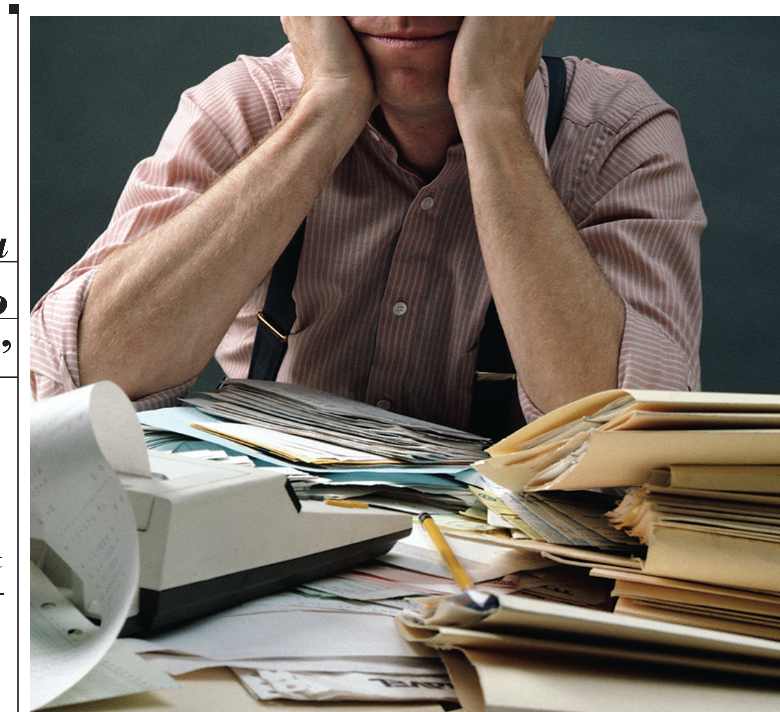
"The more complete the data set you have the fewer assumptions you have to make."

on projected equipment and driver activity levels and productivity. When this information is not known and simply estimated, problems quickly surface.

Shippers often aren't aware of how their loading and unloading practices affect carrier networks or how carriers deal with unplanned events such as weather emergencies, product recalls and labor disruptions.

Management is not going to approve any program that does not have a well-substantiated return on investment analysis supported by strong, in-depth data. Palmer suggests that the information provided to carriers should include: Lane volumes by period with variations in lane volumes by season; carrier capacity availability; current rates per lane; load/unload turn times for origins and destinations; impacts on distribution center shipping and receiving labor costs if turn times are too lengthy; the number of open jaw lanes; opportunities for third-party for-hire freight on those lanes to neutralize the cost penalty; safety stock reduction opportunities; and the dedicated carrier's proposed operating costs. "It is critical that this be assessed within the context of future plans for the company's supply chain network, making certain the environment doesn't change soon after implementation," Palmer says. "Most companies sophisticated enough to be considering a contract carriage/dedicated fleet solution have a sufficiently detailed and reliable data bank of information at hand to build the analysis. If they don't, then they need to take the time to find out how their operations really

"Leaps of faith on a fool's hope is no way to run an operation."



perform. Leaps of faith on a fool's hope is no way to run an operation."

Newbourne stresses the need to understand and develop detailed operational information before going to a dedicated carrier. His list includes freight flow throughout the week; shipping windows; receiving windows; live versus drop operations; history of dwell times at origins and destinations; opportunities to slip seat drivers; operating parameters to select the right power unit and shipping characteristics to select the right trailing equipment; daily capacity requirements; length of haul; types of highway infrastructure available (Interstates, state highways, local roads, etc.); availability of qualified drivers; fleet size and associated yard support requirements; number of miles per week; and expected maintenance intervals and down time.

"The more complete the data set you have the fewer assumptions you have to make and the greater the likelihood that the resulting dedicated proposal will effectively meet the requirements of the situation," Newbourne says. "While you should never wait to have 100 percent perfect information, you do need a considerable portion to make a realistic decision. The key is to put restrictions or limitations around any proposed operation based on the degree that you had to make assumptions based on missing information."

The third question on the test is "When should you consider outsourcing instead of a private fleet?" If you answered "core competency rules," our experts would agree.

Palmer suggested that outsourcing should be considered only if there is difficulty finding/keeping quality drivers who are safe, motivated, courteous, honest and qualified; there are capital investment constraints (tractors, trailers, communications and tracking equipment); or an aversion to the safety risk or inability to find experienced management to accomplish good execution of transportation and distribution.

And the last question: "What factors should shippers use to select the contending carriers from the pretending carriers?"

If you said experience and strong management, that would be a good start, but experience and management doing what? Palmer says experience with your company's operating environment is essential, along with well-maintained newer equipment, state-of-the-art fleet management systems, an effective safety program, an equitable driver compensation package and a relatively low driver turnover ratio (i.e. an ability to hire and retain drivers).

If Paul Newbourne was grading your paper he would give you bonus points if you also included considerations such as: How many dedicated operations do they have in place today and what is their performance; What is their modeling capability to determine the design of a dedicated fleet; What is their overall safety and service performance record; What is their overall financial stability; cost per mile of their proposal; the carrier's current position in the proposed market lanes; and their willingness to do an "open book" arrangement.

Newbourne also says dedicated carriers must have the managerial talent and skill to effectively manage drivers, equipment; marketing and selling capacity to eliminate empty miles and billing and collections. Can they effectively run a trucking company? Also, can they manage the liability exposure — not just cargo liability but safety. What happens to the shipper's cargo if the dedicated carrier is shut down after a Department of Transportation audit?

Unless things have changed a lot since we went to college, the question of the day is how do you think you did? Were your answers superficial? Would you have preferred a multiple-choice test where you could have guessed some of the answers?

Dedicated contract carriage can provide some significant benefits under the right conditions. The keys to success include a strong data set, the right market conditions and well-defined and realistic goals.

Regardless of whether you are a shipper, a logistics company or a carrier, choose wisely. You are accountable for the direction in which you are leading your company, and the stakes are very high.

John A. Gentle is a veteran logistics and transportation expert, with four decades of experience at major shippers, including 35 years at Owens Corning, where he was global leader for processes and transportation affairs. His consulting firm, John A. Gentle & Associates, Toledo, Ohio, works with shippers, 3PLs and carriers. Visit its Web site at www.relatranships.com.

Dedicated Contract Carriage