Evolution of Motor Carrier Contracting

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Abstract
The relationships between motor carriers and their shippers have changed a great deal since regulatory reform of the U.S. truck transportation industry began in the late 1970s. Prior to this regulatory change, business activity between carriers and shippers was conducted primarily on a transactional or shipment-to-shipment basis. The operating and pricing freedoms granted to motor carriers along with the development of new technologies and processes, such as electronic data interchange (EDI) and just-in-time (JIT) production and inventory management, have encouraged carriers and shippers to form closer, longer term, and more interdependent relationships. These “partnershipping” relationships between carriers and shippers resemble the relationships between shippers and their other service and product vendors that evolved much earlier.

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Operations and Supply Chain Management

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Evolution of Motor Carrier Contracting

After deregulation, special rate and service agreement contracts between motor carriers and shippers have become increasingly popular. This article reports that in the absence of regulatory prohibitions, contracting is not resulting in abuses that restrict common carrier competition or encourage carrier discrimination against shippers.

by Charles D. Braunschweig, Michael R. Crum and Benjamin J. Allen

The relationships between motor carriers and their shippers have changed a great deal since regulatory reform of the U.S. truck transportation industry began in the late 1970s. Prior to this regulatory change, business activity between carriers and shippers was conducted primarily on a transactional or shipment-to-shipment basis. The operating and pricing freedoms granted to motor carriers along with the development of new technologies and processes, such as electronic data interchange (EDI) and just-in-time (JIT) production and inventory management, have encouraged carriers and shippers to form closer, longer term, and more interdependent relationships. These "partnershipping" relationships between carriers and shippers resemble the relationships between shippers and their other service and product vendors that evolved much earlier.

One key characteristic of partnershipping is the development of a contractual rather than a transactional relationship. Economic regulation greatly limited the ability of trucking firms to contract with their shippers. The justification for restricting motor carrier contracting was essentially to protect common carriers and to prevent carrier discrimination against shippers. The Motor Carrier Act of 1980 and subsequent Interstate Commerce Commission (ICC) rulings in the early 1980s relaxed, but did not eliminate, requirements and restrictions on contracting. The result was a substantial increase in contract motor carrier service during the remainder of the decade. Although this increase has been well documented, there has been little empirical research on the extent to which carriers and shippers established contractual relationships, the nature of these relationships, or the impacts they had on the trucking industry and shipper community.

During the early 1990s the ICC further reduced its regulation of contract carriage in response to concerns emerging from the undercharge issue. The undercharge issue involves trustees for bankrupt motor carriers billing shippers for past undercharges — the difference between the prevailing published, and
thus legal, common carrier tariff rates and the unfiled and unpublished rates charged by the now-bankrupt carriers. It has been alleged that shippers, as they became aware of this practice, often turned to contracting at the turn of the decade to avoid potential undercharge claims. However, the issue then arose as to whether the shippers and carriers had valid contracts; that is, whether the contracts met existing ICC requirements and thus provided legal rates. In subsequent legislation intended to resolve the undercharge controversy Congress also changed motor carrier contracting requirements, leading at least one analyst to conclude that motor contract carriage today is more tightly regulated than motor common carriage. This raises the question — what is the prognosis for motor carrier contracting?

The primary purpose of this article is to facilitate an understanding of contracting for trucking service and its future. To accomplish this purpose the article has two objectives: (1) to examine the extent and nature of contracting during the 1980s; and, (2) to discuss the recent legislative and regulatory changes concerning motor carrier contracting. The first objective serves the purpose by providing insights on why shippers and carriers contract and on the impact of contracting on the structure and organization of the trucking industry. The decade of the 1980s provides a good indication of what future trends and behavior in motor carrier contracting might be if there were no regulatory barriers or incentives since the ICC relaxed its regulation and the motivation for contracting during this period was unaffected by the undercharge controversy. The second objective serves the purpose by identifying potential regulatory barriers and incentives to contracting arising from recent Congressional and ICC action.

The article presents a brief review of some of the more significant early 1980s regulatory policy changes pertaining to contracting. Results of a survey of shipper and trucking firm contracting behavior during the decade are then presented, followed by a discussion of ICC contract policy and legislative changes in the early 1990s.

Key 1980s Regulatory Changes and the Industry Response

Common carrier service was the backbone of the regulated U.S. motor carrier industry. ICC regulation of contract carriage was primarily designed to control its competition with common carriage. Perhaps the most restrictive regulation was the “Rule of Eight” — contract carriers were often limited to serving no more than eight shippers or when they reached eight shippers found that further permit applications were scrutinized very closely by the ICC. Additionally, trucking firms were not, as a rule, allowed to hold “dual authority,” that is, to provide both common and contract carrier service. Though not regulated as rigorously as common carrier rates, contract rates still had to be filed and published.

By the mid-1980s the economic regulatory reform of the U.S. motor carrier industry had removed each of these key obstacles or disincentives to contracting. In the late 1970s the ICC released restrictions concerning dual authority and allowed private motor carriers (shippers that provide own truck transport) to apply for contract permits under certain circumstances. Section 10923 of the Motor Carrier Act of 1980 no longer defined contract carriage in terms of service to a limited number of
presents a brief review of some significant early 1980s regulatory changes pertaining to the results of a survey of shipping firm contracting behaviors. Findings are then presented along with a discussion of ICC contract legislation changes in 1980.

Regulatory Changes and the Response

Motor carrier service was the regulated U.S. motor industry. ICC regulation of common carriers was designed to provide competition with common carriers and was intended to regulate the most restrictive rates of shippers found limited to more than eight shippers or limited eight shippers found permit applications were reviewed closely by the ICC. ICC regulation of carriers was often limited to shippers, effectively eliminating the Rule of Eight restriction. It also gave broader sanction to dual authority. In its implementation of the Motor Carrier Act of 1980 the ICC in 1982 began to exempt individual contract motor carriers from tariff filing requirements, and in 1983 it issued a blanket exemption from all contract tariff filing requirements. In 1983, entry regulation was substantially relaxed as a significant number of industry-wide contract carrier authority permits were issued. These industry-wide or "class" permits were authorized based on service needs of the involved industry group and without the actual support of potential contracting shippers.

Requirements that remained in effect for the balance of the 1980s were specified in CFR 49 Section 1053 (as amended in 1983). This stated that contracts: "shall be in writing, shall provide for transportation for a particular shipper or shippers, shall be bilateral and impose specific obligations upon both carrier and shipper or shippers, shall cover a series of shipments during a stated period of time in contrast to contracts of carriage governing individual shipments." Also, it was required that copies of the contracts be preserved by the parties for at least one year thereafter.

Trucking firms responded quickly to these regulatory changes. An indication of the subsequent growth in contract motor carriage is provided by ICC data that show a doubling from 1980 to 1985 in the percentage of total annual Class I motor carrier revenue generated under contract from approximately four to about 8% and a threefold increase to about 12.4% by 1990 (see Table 1).

<table>
<thead>
<tr>
<th>Year</th>
<th>Intercity Class I Common Carrier Revenue</th>
<th>Intercity Class I Contract Carrier Revenue</th>
<th>Class I Contract as % of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1970</td>
<td>$10,147</td>
<td>$332</td>
<td>3.2%</td>
</tr>
<tr>
<td>1975</td>
<td>$14,268</td>
<td>$63</td>
<td>0.4%</td>
</tr>
<tr>
<td>1980</td>
<td>$26,691</td>
<td>$1,139</td>
<td>4.1%</td>
</tr>
<tr>
<td>1985</td>
<td>$29,019</td>
<td>$2,518</td>
<td>8.0%</td>
</tr>
<tr>
<td>1990</td>
<td>$36,974</td>
<td>$5,212</td>
<td>12.4%</td>
</tr>
</tbody>
</table>

*Annual Class I contract revenue decreased greatly from 1974 to 1975. This may have been due to the change in definition of a Class I carrier on Jan. 1, 1974 to $3 million annual revenue from $1 million. A number of carriers included in the 1974 data would not be included in the 1975 data.

Source: Interstate Commerce Commission Annual Reports (various years).
data after 1980 is incomplete, however, because of data filing exemptions and the failure of some carriers to comply with filing requirements. For example, in the 1990 fiscal year (ending on September 30, 1991) $5.212 billion of contract revenue was generated by the 728 Class I carriers that filed reports. Contract revenue data are missing for 135 Class I carriers.

Filing exemptions that are likely to lead to a substantial underestimation of contract revenue are granted to at least two types of carriers: carriers that derive 100% of their revenue from contract service and certain specialized (non-general freight) carriers. Data is available that shows three times more contracting at this time than reflected by the ICC's data.

The increase in the number of ICC-regulated trucking firms that have contract authority provides further evidence of the substantial growth in contracting. In 1980 only about one-third of ICC-authorized motor carriers held contract authority. By 1992 this figure had jumped to about 78%.11

The academic literature provides some additional insights to the growth in contracting, but only three studies have employed survey data from motor carriers and shippers to investigate the extent of motor carrier contracting activities. Only one of these studies used a representative sample of trucking firms. A brief summary of each follows.

In 1987 LaLonde and Cooper surveyed 311 shipper and 85 carrier members (the majority were motor carriers) of the Council of Logistics Management (CLM). Given the sampling methodology, the authors acknowledged findings of their study would not be representative of the population of shippers and carriers but would instead represent leading-edge business practices. Their findings revealed that shippers, on average, expected to increase their percentage of volume shipped by contract motor carrier from 16.8% in 1987 to 20.4% in 1990. Carriers expected the percentage of their revenues derived from contract carriage to increase from 26.9% to 31.1% over the same period of time.12

In 1990 LaLonde and Masters surveyed traffic managers, logistics executives and carrier sales executives as part of a major study to explore the changing nature and scope of the corporate transportation function. Questionnaires were sent to 628 shipper members of the American Society of Transportation and Logistics (AST&L) and the CLM, and to 218 trucking members of the Sales and Marketing Council of the American Trucking Associations. The authors received 211 usable responses from shippers and only 30 usable responses from carriers. They found that the use of contract rates increased dramatically during the 1980s and by 1990 almost 50% of freight movements were handled under contract rates. It was estimated that by 1995, between six and seven shipments out of ten would be moving under contract rates.13

Crum and Allen conducted two studies that looked at contracting in the context of a larger research question pertaining to carrier-shipper relationships. In these studies, one based on a representative survey of motor carriers14 and the other based on a survey of mostly large manufacturing shippers,15 they examined a number of relationship components observed in partnerships activities, including EDI and dependence on primary shippers and primary carriers.

This article's research expands upon the earlier work of Crum and Allen by focusing solely on the contracting data generated in these studies. As noted earlier, because the data collection pre-
The emergence of the undercharge issue as a major concern to shippers, valuable insight to the nature and underlying benefits of contracting can be gained. Stated differently, these data will not, in general, reflect the use of contracts for the purpose of alleviating or avoiding what is likely to be a regulatory aberration, (as a legal defense to undercharge claims or as a means of avoiding potential future undercharge liabilities). Consequently, the data provide a good indication of the extent of contracting in 1989 and the expected level of contracting by 1995.

**Contracting In The 1980s**

Data presented in the following sections were obtained from surveys mailed to shippers and trucking firms in 1989 and 1990. Questionnaires were mailed to the 412 shipper members of the AST&L and to 800 randomly selected firms listed in the *Official Directory of Industrial & Commercial Traffic Executives*. From the 1,181 delivered questionnaires, 214 usable responses were obtained for an effective response rate of 18.1%. Similar questionnaires were mailed to 1,200 randomly selected U.S. Class I and Class II motor carriers listed in the *National Motor Carrier Directory*. From the 1,183 delivered questionnaires, 266 usable responses were received for an effective response rate of 22.5%.

Shippers respondents tended to be large firms as nearly half had 1988 sales revenue in excess of $1 billion and 40% had sales revenue between $100 million and $1 billion. More than two-thirds of the respondents listed their primary function as manufacturing or processing, with the remainder being in distribution or retailing.

The sample of 266 Class I and II motor carriers represents approximately 13.5% (266 of 1,968) of the population, 14.1% of all Class I motor carriers (119 of 846) and 13.1% of all Class II motor carriers (147 of 1,122). Furthermore, the carrier respondents seem representative of the population with respect to characteristics of size, age and nature of operation (truckload or less-than-truckload). Nearly three-fourths of the Class I respondents had a 1989 operating revenue level between $5 million and $25 million and about 15% were in the $25 million to $100 million range. 21% of the respondents began motor carrier operations after 1980, 21% started up between 1970 and 1980, inclusive, and 58% began operations before 1970. Of the 214 respondents who clearly indicated their shipment size focus, 151 (70.6%) were primarily TL carriers and 63 (29.4%) were primarily LTL carriers.

The motor carrier survey data are used to address a traditional public policy issue: the effect of increased motor contract carriage on motor common carriage. This policy issue was examined by analyzing the level or extent of contracting, whether contracts tended to restrict the carriers' service offerings, and whether carrier size affected contracting. The size issue is addressed by comparing Class I and Class II carriers' responses for behavioral and perceptual differences. Both shipper and motor carrier data are used to explore the nature of contractual relationships and why the parties contract.

**Extent of Contracting.** 82% of motor carrier respondents (218 out of 266) reported providing some form of contract service in 1989. Of these 218 carriers, a slightly higher percentage of Class I carriers (87%) than Class II carriers (78%) were involved in contract carriage. On average, each carrier engaged in contracting generated about 41% of its 1989 annual operating revenue from...
shippers under contract. Additionally, the weighted average percentage was also about 41% — meaning that 41% of the revenue earned collectively by respondents who contract came from their shippers under contract.

Assuming that the survey respondents are representative of the population of Class I and Class II motor carriers (as they appear to be), total 1989 contract revenue can be estimated for all Class I and Class II motor carriers. As Figure 1 indicates, a total revenue amount of $66.84 billion for 1989 is estimated for all Class I and Class II carriers. Given that contracting revenue as a percent of total sample (contracting and non-contracting firms) revenue was found to be 37.4%, the estimated population revenue from contract shippers is $24.98 billion. It is further estimated that $24.02 billion (96%) of these contracting revenues were earned by Class I carriers, while the remaining $0.96 billion (4%) of contracting revenues were earned by Class II carriers.

Surveyed carriers were also asked to indicate how they expected contract revenues as a percentage of total revenues to change between 1990 and 1995. Nearly two-thirds of all respondents expected an increase in the percentage of revenue under contract by 1995, but there was a significant difference (at the 5% level of confidence) between Class I and Class II carriers in terms of the degree of increase with Class II carriers expecting a smaller increase. Less than
4% of all respondents anticipated a decrease in percentage of revenue from contracting by 1995.

**Restrictive Nature of Contracting.** The specific terms of a contract, as well as the contract's duration, can affect the extent to which a contract carrier is restricted to providing service to a certain shipper. This may adversely affect a trucking firm's ability to provide common carrier service if it functions as a dual operator.

Table 2 reveals that less than 2% of all Class I and Class II carrier respondents involved in contracting reported that they had an exclusivity clause that prohibited their firms from serving other shippers. In addition, less than 1% reported that they had a limitation on the number or type of other shippers that their firms may serve. However, roughly 50% of Class I and 40% of Class II carriers indicated their firms were required to dedicate certain equipment to meet the contracting shipper's service needs. These three items are considered to be restrictive of the carrier's ability to serve other shippers with the first two items being considered the most restrictive.

With respect to contract duration, 82 of the 102 (80%) Class I carrier respondents and 78 of the 115 (68%) Class II carrier respondents reported that a majority of their contracts were between one and two years duration. Each group reported that contract durations of less than one year and greater than two years were about evenly distributed.

**Effect of Carrier Size on Contracting.** Though the vast majority of Class II carriers were engaged in contracting, more than half of both Class I carriers (59 out of 103) and Class II (63 out of 115) carriers believed that carrier size was a factor in the willingness of shippers to contract with a given carrier. However, for the statement that shippers are more willing to negotiate contracts

### TABLE 2: TERMS INCLUDED IN THE MAJORITY OF CLASS I AND CLASS II CARRIER CONTRACTS

<table>
<thead>
<tr>
<th>Terms</th>
<th>Total Sample</th>
<th>Class I Carrier Responses</th>
<th>Class II Carrier Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exclusivity Clause</td>
<td>4 (1.8)</td>
<td>2 (1.9)</td>
<td>2 (1.7)</td>
</tr>
<tr>
<td>Limitation on Other Shippers</td>
<td>2 (0.9)</td>
<td>1 (1.0)</td>
<td>1 (0.9)</td>
</tr>
<tr>
<td>Dedication of Equipment</td>
<td>97 (44.5)</td>
<td>51 (49.5)</td>
<td>46 (40.0)</td>
</tr>
</tbody>
</table>

n = 218 103 115

1 Partial list of terms provided in carrier survey.
with larger motor carriers, both Class I and Class II carriers had mean rating scores that fell in the "neutral zone" (mean scores near 4.0 on a 7 point scale). The carrier groups differed slightly on their statement that larger motor carriers are able to negotiate more economically favorable contracts with shippers. While Class II carriers express a stronger disagreement to the latter statement, the difference was not large enough to be statistically significant.

**Shipper and Carrier Perspectives on Contracting.** As previously noted, carriers and shippers have created new formalized relationships that rely heavily on contract motor carrier service. The changing dynamics of this contractual relationship between carriers and shippers are important to practitioners involved in both traffic and carrier management. This section explores the impact that increased contract carriage may have on the interests of these practitioners by analyzing the nature and scope of contracting, the means of obtaining shipper business by contracting, and the benefits of contracting.

**Nature and Scope of Contracting.** Table 3 shows items included in the majority of contracts between carriers and shippers. For the entire sample of carrier and shipper respondents, the three items most often included in con-

<table>
<thead>
<tr>
<th>Terms</th>
<th>Total Sample</th>
<th>Shipper Responses</th>
<th>Carrier Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exclusivity Clause</td>
<td>6 (1.4)</td>
<td>2 (0.9)</td>
<td>4 (1.8)</td>
</tr>
<tr>
<td>Limitation on Other Shippers</td>
<td>5 (1.2)</td>
<td>3 (1.4)</td>
<td>2 (0.9)</td>
</tr>
<tr>
<td>Dedication of Equipment</td>
<td>175 (40.5)</td>
<td>78 (36.4)</td>
<td>97 (44.5)</td>
</tr>
<tr>
<td>Rate Discounts for Failure to Meet Service or Quality Levels</td>
<td>60 (13.9)</td>
<td>43 (20.1)</td>
<td>17 (7.8)</td>
</tr>
<tr>
<td>Due Dates for Freight Bill Payments</td>
<td>200 (46.3)</td>
<td>93 (43.5)</td>
<td>107 (49.1)</td>
</tr>
<tr>
<td>Procedures for Settling Freight Claims</td>
<td>198 (45.8)</td>
<td>103 (48.1)</td>
<td>95 (43.6)</td>
</tr>
<tr>
<td>Guaranteed Freight Volumes</td>
<td>166 (38.4)</td>
<td>72 (33.6)</td>
<td>94 (43.1)</td>
</tr>
</tbody>
</table>

1Contract terms provided in carrier and shipper surveys.
MOTOR CARRIER CONTRACTING

Tracts were due dates for freight bill payments, procedures for settling freight claims, and dedication of equipment by the carrier to meet shippers' needs. The two most restrictive items, from the motor carriers' perspective, were the items least likely to be included in a contract between carriers and shippers. Less than 2% of all carrier and shipper respondents indicated that an exclusivity clause that prohibits a carrier from serving other shippers or a clause limiting the number of shippers a carrier may serve were included in contracts between the two groups.

Responses of carriers and shippers were not always consistent with one another since surveyed carriers were serving shippers other than those surveyed. Shipper respondents revealed procedures for settling freight claims were most often included in their contracts, while due dates for freight bill payment were most often included in contracts of carrier respondents. The contract term having the greatest discrepancy between carriers and shipper respondents was carrier rate discounts for failure to meet service or quality levels. 20% of the shippers reported inclusion of rate discounts tied to service performance compared to about only 8% of the carriers. This may indicate that smaller shippers did not have as much

<table>
<thead>
<tr>
<th>Benefits</th>
<th>Total Sample</th>
<th>Class I Carriers</th>
<th>Class II Carriers</th>
<th>t-stat</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ability to Tailor Service Levels</td>
<td>5.340</td>
<td>5.250</td>
<td>5.420</td>
<td>-0.854</td>
<td>0.395</td>
</tr>
<tr>
<td>Improved Planning for Equipment</td>
<td>5.313</td>
<td>5.079</td>
<td>5.522</td>
<td>-2.187</td>
<td>0.029</td>
</tr>
<tr>
<td>Better Able to Price Service</td>
<td>5.028</td>
<td>4.911</td>
<td>5.134</td>
<td>-1.092</td>
<td>0.276</td>
</tr>
<tr>
<td>Guarantee Freight Volume/Revenue Base</td>
<td>5.023</td>
<td>4.881</td>
<td>5.150</td>
<td>-1.207</td>
<td>0.226</td>
</tr>
<tr>
<td>Improved Planning for Labor</td>
<td>4.822</td>
<td>4.525</td>
<td>5.089</td>
<td>-2.595</td>
<td>0.010</td>
</tr>
<tr>
<td>Reduce Shipper from &quot;Shopping Around&quot;</td>
<td>4.682</td>
<td>4.604</td>
<td>4.714</td>
<td>-0.467</td>
<td>0.697</td>
</tr>
<tr>
<td>Confidentiality of Rates</td>
<td>4.443</td>
<td>4.444</td>
<td>4.442</td>
<td>0.008</td>
<td>0.936</td>
</tr>
</tbody>
</table>

1 A rating scale of 1 to 7 was used where 1 = not important, 4 = moderately important, and 7 = extremely important.

The mean ratings are reported in this table.
TABLE 5: COMPARISON OF CARRIER AND SHIPPER BENEFITS FROM CONTRACTING

<table>
<thead>
<tr>
<th>Benefits</th>
<th>Total Sample</th>
<th>Shippers</th>
<th>Carriers</th>
<th>t-stat</th>
<th>P-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ability to Tailor Service Levels</td>
<td>5.411</td>
<td>5.497</td>
<td>5.340</td>
<td>-1.052</td>
<td>0.294</td>
</tr>
<tr>
<td></td>
<td>n=175</td>
<td>n=212</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Improved Availability/Planning</td>
<td>5.265</td>
<td>5.207</td>
<td>5.313</td>
<td>0.690</td>
<td>0.490</td>
</tr>
<tr>
<td>of Equipment</td>
<td>n=174</td>
<td>n=214</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Better able to Price Service</td>
<td>5.257</td>
<td>5.534</td>
<td>5.028</td>
<td>-3.409</td>
<td>0.001</td>
</tr>
<tr>
<td></td>
<td>n=176</td>
<td>n=213</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Confidentiality of Rates</td>
<td>4.665</td>
<td>4.932</td>
<td>4.443</td>
<td>-2.662</td>
<td>0.008</td>
</tr>
<tr>
<td></td>
<td>n=176</td>
<td>n=212</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The mean ratings are reported in this table.

A rating scale of 1 to 7 was used where 1 = not important, 4 = moderately important, and 7 = extremely important.

Negotiating strength or leverage as larger shippers (as shipper respondents tend to be large manufacturing firms, the discrepancy between these two percentage figures may reflect exclusion of service-related rate discounts from the smaller shippers served by surveyed carriers).

Contracting as a Means of Obtaining Shipper Business. The importance of a motor carrier’s willingness to provide contract service when the shipper is making its carrier selection decision was considered to be at least moderately important (i.e., importance rating of 4.0 or greater on a seven point scale) by both carriers and shippers. No significant difference was found between the carriers’ rating of 4.99 and the shippers’ rating of 4.90.

Over 34% of motor carrier respondents indicated that contracting was a requirement of the shipper. Further segmentation reveals that 42% (43 out of 103) of Class I carriers and 28% (32 out of 115) of Class II carriers encountered such a requirement from most of their contracting shippers.

Benefits of Contracting. Carrier respondents’ average importance ratings of the benefits from contracting are reported in Table 4. All benefits were viewed as at least moderately important. The two most important carrier benefits from contracting were the ability to tailor service levels and improved planning for equipment. As Table 4 indicates, Class I and Class II carriers were in agreement with respect to their ratings of the importance for all but two of the benefits from contracting. Significant differences existed for the benefits of improved planning for labor (at the 1% level of confidence) and improved planning for equipment (at the 5% level of confidence). Class II carriers assigned more importance to these benefits than did Class I carriers.
motor carriers and 28% (32 out of 112) of Class II carriers encountered resistance from most of their shippers.

of Contracting. Carrier average importance ratings from contracting are given in Table 4. All benefits were viewed at least moderately important. Significant differences (at the 1% level of confidence) between carrier and shipper mean ratings were found for both confidentiality of rates and ability to better price service. Shippers assigned more importance to these contract benefits than did carriers.

ICC Contract Policy And Legislation In The Early 1990s

Contracting was obviously a popular method for purchasing motor carrier service during the 1980s. During this period the ICC relaxed both its regulations pertaining to and its oversight of motor contract carriage. The 1990s have witnessed a complete turnaround in contract policy as the ICC further reduced its requirements only to have Congress later reinstate previous requirements and add new ones.

In the early 1990s a number of cases arose in which representatives of bankrupt motor carriers filed undercharge claims on traffic that had moved under contract on the basis that the contracts were invalid because they were not in strict compliance with ICC regulations. Several of these cases involved dual authority carriers where legally defective contracts potentially subjected shippers to the carriers' published (common carrier) rates. In these cases the ICC ruled to protect the shipper when it appeared that the parties' intent was to transport the freight under the carrier's contract permit (rather than its common carrier certificate), but against the shipper in other cases. To protect shippers moving freight under contract from potential undercharge claims, the ICC repealed its contract regulations effective June 20, 1992. With respect to legal requirements, this left only the statutory requirements in U.S.C. 49 Section 10102(15)(E) that define a motor contract carrier as one that provides motor vehicle transport service for compensation under continuing agreements 'by assigning motor vehicles for a continuing period of time for the exclusive use (of the shipper or shippers) or ... designed to meet the distinct needs of each (shipper).'

Congress finally became involved with the undercharge controversy and approved the Negotiated Rates Act of 1993 (NRA) on December 3. In this act, which went into effect on March 2, 1994, Congress reconstructed and expanded requirements of the ICC's former regulations pertaining to the form and content of contracts. The NRA (in amended U.S.C. 49 Section 10702) established that, at a minimum, contracts shall: (1) be in writing; (2) identify parties thereto; (3) commit the shipper to tender and the carrier to transport a series of shipments; (4) contain contract rate or rates for the transportation service to be or

Table 5 shows the comparison of average importance ratings of the benefits from contracting for both shipper and carrier respondents (the aggregate of Class I and Class II carriers). Again, benefits were viewed as being at least moderately important. Consolidating the entire sample of carrier and shipper mean ratings reveals that the ability to tailor service levels was the single most important benefit from contracting, while confidentiality of rates was the least important benefit. However, significant differences (at the 1% level of confidence) between carrier and shipper ratings were found for both confidentiality of rates and ability to better price service. Shippers assigned more importance to these contract benefits than did carriers.

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\[\text{ICC Contract Policy And Legislation In The Early 1990s}\]

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being provided; and (5) state that it provides for the assignment of motor vehicles for a continuing period of time for the exclusive use of the shipper; or state that it provides a service designed to meet distinct needs of the shipper.

The first three items listed above were ICC rules in place during the decade of the 1980s. The fourth item restored a requirement that was eliminated when the ICC abolished tariff filing for contract carriers in the early 1980s. The last item is a new requirement — the contract must state which of the two alternative contract carriage definitional criteria is being met. Additionally, under the NRA motor contract carriers are required to retain the written agreements for a minimum period of 3 years, and the ICC is required (effective May 1994) to conduct periodic random audits to ensure motor contract carriers are complying with its requirements and are adhering to rates set forth in the contracts. However, NRA does not require carriers to file their contracts with the ICC. The Trucking Industry Regulatory Reform Act of 1994 (TIRRA) codified this tariff filing exemption for contract carriers.24

Though the NRA would seem to eliminate any confusion about what constitutes a legal contract, the ICC's interpretation of the statute as delineated in Ex Parte No. MC-198 (Sub-No.1), Policy Statement in Motor Contract Requirements Under the NRA, dated February 28, 1994, seems less clear. For example, the ICC does not establish a clear standard for what constitutes "a series of shipments." It acknowledges isolated shipments or spot transportation do not satisfy the requirement, but short-term (week-long agreements or requirements) contracts will suffice. The ICC also interprets the statute as requiring that parties need only indicate which definitional criteria of contract carriage is being met, but they need not detail how those criteria are being met (though the ICC then goes into a long discussion of how easy it is to show that the distinct needs requirement is met). The ICC also takes a broader view of the statutory language concerning inclusion of rates. Rather than stating the actual rate, the contract may provide a methodology for determining the rate.25 At least one analyst construes the ICC's policy to mean "that it will be business as usual in the area of contract carriage."26

The impact of these statutory and regulatory gyrations and mixed signals coming from Congress and the ICC upon the propensity of shippers to contract for motor carrier service is difficult to project. Certainly, the more confusion there is about what constitutes a valid contract and the greater the risk associated with invalid contracts, the more hesitant shippers will be to contract. Further complicating the picture is another significant piece of regulatory reform legislation, the TIRRA, which may influence indirectly the attractiveness of contracting.

The TIRRA eliminates the tariff-filing requirement for motor common carriers using an individually determined rate, classification, rule or practice. Carriers are required to furnish the shipper, upon request, a copy of the rate classification, rules and practices upon which the rate agreed to may have been based. The ICC decides rate disputes based on the record before it.

Though viewed favorably by most shipper groups, a number of interested parties have expressed concern that shippers may incorrectly believe tariffs have been eliminated and that rate negotiation and determination will be a simple process. Rather, they see the carriers' rules tariffs being a potential major problem.27 These rules may include, for
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Of these statutory and rules and mixed signals transport and the ICC upon shippers to contract for service is difficult to probe the more confusion there constitutes a valid contract to the risk associated contracts, the more hesitant to contract. Further picture is another significance the ICC upon shippers and carriers, which may influence practicability of contract-

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er, they see the contracting a potential major rules may include, for example, restrictions on rates and discounts, credit rules might void discounts for late payment, accessorial charges, liability limitations and a variety of other charges and penalties. 28

Thus, contracting might be viewed as a preferred method for establishing rates in the new pricing environment.

Conclusion

During the last few years of the 1970s and the first half of the 1980s the ICC implemented significant reductions in its regulation of motor carrier contracting. Data collected by the ICC indicated a subsequent large increase in trucking revenue generated under contract. Missing from the data base, however, were a number of trucking firms that were likely to be very active in contracting. The survey data reported in this article shows that contracting was much more pervasive than the ICC data indicated and continued growth in contract activity was expected by the carriers.

By the end of the 1980s Class I and II motor carriers were heavily involved in contracting. When contracting carriers are grouped with non-contracting carriers, nearly 30% of all revenue earned by the surveyed firms was derived from contract freight. While the percentage of surveyed carriers (82%) engaged in contracting was nearly identical to what the ICC reported in 1992 (78%), the estimated $24 billion of contract revenue for all Class I carriers in 1989 greatly exceeds the $5.2 billion reported to the ICC in 1990.

The use of contracting was expected to be even greater in the future as nearly two-thirds of all carrier respondents expected an increase in the percentage of revenue under contract by 1995. This expectation was expressed before the emergence of the undercharge controversy, the subsequent increase in contract regulatory requirements, and the end of the filed rate doctrine as enacted in the PHYRA. The future of contracting depends on the inherent benefits it provides to both shippers and carriers, the impact that the new regulations have on these benefits, the difficulties encountered in meeting the new regulatory requirements, and the effect it has on the availability of common carriage service (since a severe adverse effect might lead to greater restrictions being legislated).

Survey results indicate contracting produced a number of benefits for both shippers and carriers. On average, both the carrier and shipper respondents perceived each of the benefits listed in the survey to be at least moderately important, though some differences between shippers and carriers were noted. Shippers assigned significantly greater importance to the benefits of confidentiality of rates and ability to better price service than did carriers. Elimination of filed rates may lessen the benefit of confidentiality, but as discussed in the preceding section, contracting may be a "safer" way for shippers to establish rates in the new pricing environment.

Further evidence that contracting produces benefits was indicated by its importance in the carrier selection process. Both carriers and shippers reported that the carrier's willingness to provide contract service was an impor-
tant consideration when shippers were selecting their carriers. Indeed, a large percentage of carrier respondents reported that contracting was a requirement of the shipper, implying that contracting was often initiated by the shipper. Shippers were demanding contract service, and motor carriers had to provide this service or risked losing the shippers' business.

While individual contracts may address a number of operating and financial issues, the two most commonly included terms in the respondents' contracts dealt with financial issues. Due dates for freight payment and procedures for handling freight claims were cited as the two most often included terms in the majority of contracts. The TIRRA increases the importance of negotiating and documenting these and other rules and practices associated with the agreed rates.

Provisions for dedicated equipment and guaranteed freight volume were also popular, ranking third and fourth, respectively, and appeared in the majority of the contracts of nearly 40% of all respondents. Thus, it appears a substantial number of carriers and shippers were meeting the current requirement that contracts must state which definition of contract carriage is being used.

Finally, contracting was investigated from a public policy perspective as the restrictive nature of contracting and the effect of carrier size on contracting were investigated. The terms of most carrier-shipper contracts did not include the most restrictive types of provisions, exclusivity clauses or limits on serving other shippers. On the other hand, about 45% of carrier respondents provided dedicated equipment to their shippers. While this is restrictive in the sense that it removes equipment from potentially being used in the performance of common carriage, current regulation requires contracts include either dedicated equipment or meet the distinct needs of shippers. A large percentage of carrier respondents indicated the majority of their contracts had a one- to two-year duration. This would imply that carriers were not restricted by the duration of their contracts.

The majority of carrier respondents expressed the opinion that carrier size was a factor in the willingness of shippers to contract with a given carrier, but neither Class I nor Class II carriers perceived shippers to be more willing to negotiate with larger carriers or that larger carriers were able to negotiate more economically favorable contracts. Since neither carrier class perceived a disadvantage for the smaller carriers, and since 78% of the surveyed Class II carriers were engaged in contracting, the size of carrier does not appear to have been a problem when negotiating with contract shippers.

In summary, results of this study indicate contracting for motor carrier service was pervasive after most regulations pertaining to contracting were eliminated. Contracting was expected to increase even more because of the substantial benefits it produces. Furthermore, contracting did not appear to affect adversely the availability of common carriage service. Finally, the current legislative and regulatory requirements do not appear to negate the benefits or reasons for contracting nor to be so burdensome as to discourage contracting.
This is restrictive in the way the ICC removes equipment from being used in the performance of common carriage, current requirements contracts include furnished equipment or meet the needs of shippers. A large percentage of carrier respondents indicated that some of their contracts had a shorter duration. This would indicate that carriers were not restricted by their contracts.

Only 45 of carrier respondents expressed an opinion that carrier size influenced the willingness of shippers to contract with a given carrier, but the majority of Class II carriers perceived them to be more willing to contract with larger carriers or that carriers were able to negotiate more favorably.

Carriers of the smaller carriers, the majority of the surveyed Class II carriers engaged in contracting, the ICC does not appear to have been active when negotiating with these carriers.

The results of this study indicated that for motor carrier contracting to be pervasive after most regulatory barriers to contracting were removed because of the substantial benefits it produces. Further enforcement did not appear to indicate any change in the availability of contract service. Finally, the current and regulatory requirements appear to negate the benefits of contracting nor to be expected to discourage contracting.

Endnotes


4. Since common carriage was generally subjected to more rigorous regulation, the ICC was concerned with attempts by common carriers to circumvent regulation by seeking contract authority. Contract permits were intended for those carriers offering more specialized services or equipment to more limited potential shipper markets. In such markets carriers and shippers were deemed have fair equal bargaining power and arms length negotiation was considered appropriate. Consequently, regulation of rates and routes was less stringent than for common carriers.


16. Class I carriers were defined at that time as carriers that generated at least $5 million annual revenue. Class II carriers generated at least $1 million annual revenue but less than $5 million.

17. The 1990 data on the number of Class I and II motor carriers were obtained from the Interstate Commerce Commission, Office of Economics, Division of Audit and Accounting.

18. The basic assumption is that the revenue estimated for the carriers in the sample is equal to 13.5% of the total revenue of all Class I and Class II carriers.


21. Augello, p. 11. An excellent review of the various criteria used by the ICC in these cases is presented by Augello on pages 34-38.


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section 10702(b).

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29. Cawthorne, p. 11.

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