Rolling the Dice on Import Cargo

Why the use of independent drivers for port drayage is a risk that large importers can't afford to take.

Introduction

Most port drayage – moving containers to and from seaports – is handled by independent drivers, also called owner-operators. Because this trucking service is highly price competitive, trucking companies contract with these owner-operators to avoid taxes, healthcare coverage and other overhead that hikes costs.

The customers of these non-asset-based trucking companies, including some of the country's largest importers, are at significant risk due to this dependence on owner-operators – whether they know it or not.

In the coming years, increasing regulations and other trucking industry trends will reduce dray capacity and service quality and greatly increase financial liability for beneficial cargo owners (BCOs) that continue to rely on owner-operators, either directly or indirectly.

Why are BCOs at risk?

Let's look at the forces that are putting the squeeze on owner-operators and why BCOs are at risk.

Large-volume importers are very dependent on reliable dray capacity. When containers sit at the port, importers can rack up tens, even hundreds, of thousands of dollars in demurrage charges, not to mention the lost sales from empty store shelves. The pressure is on global transportation managers to get these containers off port and onto a store shelf as soon as possible.

When an importer uses a non-asset based dray carrier to move these containers, they rely, in essence, on a "virtual fleet" of individual owner-operators. These "on call" independent drivers can decide to simply not show up on any given day. They are not a dependable source of ongoing capacity.

Historically, there have been enough owner-operators to plug any capacity holes, but that's changing as the number of owner-operators – currently 350,000 in the U.S. – is shrinking. BCOs simply cannot rely on dray capacity like they used to. And they know it. It's one of the reasons that large importers typically contract with multiple companies for dray. No one trucking company will guarantee capacity – unless that company is asset based.

Why are there fewer and fewer owner-operators at the port? One reason is the increase in regulations.

Hours of service regulations are reducing drivers' potential earnings, and the government is strictly enforcing these HOS rules with mandatory electronic logging devices.

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Regulations are also attacking the expense line of an owner-operator's P&L, with mandates to upgrade to the most fuel-efficient tractors at a cost, according to the EPA, of about $12,800 for drivers with older vehicles.

Because of the high concentration of trucks around port operations, ports have been particularly aggressive in phasing out older, "dirtier" trucks – the very trucks that many independent dray operators use to stay competitive on these price-sensitive runs.

Starting in 2017, the Port of New York/New Jersey no longer allows trucks with engines older than 2007 to start operation at the port.

At California ports, that 2007 engine limit has been in place since 2012.

All of these regulations, whether they reduce revenue or jack up overhead expenses, combine to paint a bleak picture for future owner-operator profitability. It's why many are leaving, and fewer are joining their ranks. This trend is a real problem when you consider that the dominant model for port drayage in the U.S. is owner-operator dependent.

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Reduced Quality, Increased Liability

Large importers who view dray services as a commodity put price pressure on carriers, and that flows down to the independent driver. To get the business, these drivers quote bare-bones rates, even while regulators are demanding they invest more in equipment upgrades.

What gets dropped is the ongoing maintenance that keeps your freight moving down the road efficiently, safely and damage-free. Unsafe vehicles are involved in more accidents, and liability issues stemming from these accidents are further complicated by the owner-operator model.

In an owner-operator model, could liability for accidents fall to the importer?

Let's take workman's comp insurance, for example. Trucking companies want to avoid this cost because it adds 20% to the cost of a load. Drivers know this and forgo this important coverage to maintain favored status with their trucking company customers.

As for general liability coverage, owner-operators secure the minimum coverage possible. Most carriers require $1 million. In this scenario, what happens if someone is seriously hurt or killed in a road accident caused by the driver? Who is liable and capable of providing financial restitution?

Not the owner-operator, who holds the minimum amount of insurance required and lacks financial wherewithal.

Not the trucking company, who pushes coverage responsibility to the owner-operator.

That leaves the BCO. Does liability then fall to this importer who is contracting for the regular dray hauls?

Some importers are unaware of the risks inherent in an indirect dependence on owner-operators. Others are aware and simply turn a blind eye in the quest for the lowest rate.

Misclassification of drivers as "independent" will threaten carriers, as well as shippers

Carriers hire drivers as independent contractors to reduce costly overhead. They depend on this model to be profitable, and the owner-operators are happy to get the business, so it works for all parties – including shippers, who pay a reasonable rate for dray service.

While most owner-operators value and protect their status as independent, a segment of that community believes they are anything but, and have fought and won in court to re-classify them as company drivers. Their arguments center around the fact that carriers, and even the BCOs, dictate what runs they accept, even what routes to take to arrive at their destination – essentially treating them exactly as employees.

And guess what? The courts agree. The most prominent example is the $228 million settlement by FedEx, which used the independent contractor model as a foundation of its business model.

Drivers for Pacific 9 Transportation and other short-haul companies went on strike several times demanding to be given all the rights and benefits of employees, including the right to bargain collectively as part of a union. In 2014, the National Labor Relations Board declared that these drivers were indeed employees subject to labor laws and the right to organize.

If you are a large shipper, you may feel a step removed from these events since you may not have a direct contractual relationship with the owner-operator.

You'd be wrong.

FedEx paid out $228 million to "misclassified" owner-operators.

Witness Macy's, which contracted with two logistics companies to provide Dedicated Contract Carriage (DCC) services for home delivery. The court agreed with the independent drivers that they should have been classified as employees of the logistics companies they drove for, and then went a step further, declaring that they should have been classified as *Macy's employees* [see Fuentes V. Macy's West Stores, Inc., No. 2:14-cv-00790 (C. D. Cal. Mar. 16, 2015)].

The logistics companies and Macy's had to settle for $6.8 million. And Macy's ended up paying the bulk of that settlement because it asked for things like Macy's decals on truck doors, a driver dress code and adherence to Macy's-defined routing.

Granted, hauling a container from the port to a DC is a lot different than scheduled store deliveries, but the principle is the same. Independent drivers are often assigned to specific importers with specific shipper-related requirements.

We are entering a new era of labor law where courts will be sensitive to carriers and, by extension, BCOs that want the benefits of dedicated drivers without the taxes, benefits, insurance and other financial obligations associated with a full-time employee.

Will importers pay a lesser rate if owner-operators are moving their containers versus an asset-based trucking company? Perhaps, but not always.

Either way, is it worth the potential liability nightmare and financial risk?

Importers should align with asset-based dray companies to guarantee capacity without the risk associated with the independent port driver model.

Comparing Two Models of Dray Management

	OWNER-OPERATOR	ASSET-BASED
CAPACITY	*In theory, limitless since model uses capacity of open market. In practice, constrained. Decreasing number of owner/ operators at port. Also, drivers have freedom to turn down loads.*	***Strong, predictable capacity. Dispatch wants to drive as much business as possible to utilize available capacity. Drivers lack flexibility to turn down loads.***
COST	*Potentially less expensive model since non-asset based carriers use owner-operators to avoid local taxes, healthcare costs and insurance*	***May be more expensive model, but higher quality, lower risk solution. Carriers are fully insured.***
TRUCK	*Less reliable trucks. Minimum investments in equipment to lower overhead and be more price-competitive.*	***More reliable, late-model trucks that are well maintained since carrier wants to drive good CSA score.***
CHASSIS	*Do not own chassis and must rely on chassis pools and other sources. Could result in delays.*	***Own and maintain chassis. Results in predictable capacity when needed.***
INSURANCE	*Minimum coverage.*	***To protect their assets, providers are fully insured with coverage far superior to owner-operator model.***
RISK	*Liability issues murky in the event of a major accident that leads to injury or death. BCOs could become liable.*	***BCOs shielded from liability by carrier's comprehensive insurance coverage.***
CSA SCORES	*Carrier CSA scores not impacted if use owner-operators with a dangerous driving record. Owner-operators are independent of the carrier.*	***Significant interest in maintaining equipment quality and compliance in order to drive good CSA score.***

Time for a Shift?

For importers, if the lowest dray rate is what you want, regardless of risk, then it makes sense to rely on owner-operators and the non-asset-based trucking companies that use them. But cost pressures and regulations are causing the slow, steady extinction of owner operators at the port. The model has become impractical, and its survival improbable.

Importers that want to ensure capacity should align with asset-based transportation companies who can provide guaranteed capacity without the risk associated with the independent port driver model.

For the drivers themselves, an industry shift toward asset-based drayage companies has a silver lining. Sure, they would lose a degree of independence. But becoming a company driver brings greater security, a benefits package, a retirement fund, and maybe even an employee stock ownership plan, which some carriers are now offering to spur recruitment and retention.

Eventually, owner-operator drivers will go the way of the American cowboys of the late 1800s. They won't go away altogether, they'll just be a lot tougher to find.