InterConnect
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In This Issue...

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Got Those Deregulation Blues

Now that the dust is beginning to settle from the battle in Congress over the highway funding bill (now known as the *Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users or* "SAFETEA-LU"), we are learning that the final Bill as enacted not only authorized the spending of billions of dollars for infrastructure projects but that it also provided for a variety of substantive changes in transportation regulation.

One of the changes that has raised more questions than it has answered relates to the regulation of general freight property brokers and freight forwarders. Under the Interstate Commerce Commission Termination Act of 1995, the Federal Motor Carrier Safety Administration ("FMCSA") was required to register property brokers and freight forwarders based on a "fitness" standard. Applicants for freight forwarder authority were required to file the appropriate application with FMCSA and pay a $300 filing fee. Approval would be more or less automatic and the license would issue after the applicant filed evidence of cargo insurance and a designation of agent for service of process (BOC-3). An application for property broker authority followed the same pattern except that the regulations required a surety bond instead of the cargo insurance.

"...changes in transportation regulation... have raised questions."

Under the language adopted in SAFETEA-LU, effective October 1, 2005, the law provides that FMCSA "may" register a person to provide service as a property broker or a freight forwarder of general freight if FMCSA determines such registration is needed for the protection of shippers.[1]

What does the new language mean? FMCSA can no longer enforce its regulations regarding broker and forwarder registration. Property brokers and freight forwarders are no longer required to register with FMCSA. Brokers and forwarders are not required to have agents for service of process through FMCSA. Brokers are no longer required to file evidence of a surety bond and are relieved from their obligation to maintain records as required under previously applicable federal regulations (49 C.F.R. Part 371).[2] Freight forwarders no longer have to file evidence of cargo insurance. Although it is likely that freight forwarders continue to be liable to shippers for cargo loss and damage, such liability would be based on established case law rather than on a federal statute.

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Before DOT can decide that property brokers and freight forwarders of general freight should again be regulated, FMCSA will need to institute a rule-making proceeding to compile a record enabling the Secretary to determine that registration is required for the protection of the shipping public. If the Secretary makes such a determination, FMCSA can then promulgate rules and establish processes pursuant to which the registration may be completed.

If FMCSA wants to address the registration of brokers and forwarders, it already has a rulemaking in progress that it can use to move the project along. In May 2005, FMCSA published a Notice of Proposed Rulemaking ("NPRM") to begin the process of establishing a unified registration system for carriers, brokers and forwarders subject to FMCSA jurisdiction. However, because of the timing of the NPRM, FMCSA did not have the opportunity to request comments on the issue of whether registration of brokers and forwarders is needed for the protection of shippers. FMCSA would be required to solicit additional comments.

As of November 2, 2005, FMCSA has made no public acknowledgement of the changes regarding broker and freight forwarder registration enacted by Congress in SAFETEA-LU. Through its web page, FMCSA continues to advise prospective brokers and forwarders that they need to file for authority. Any application for broker or freight forwarder authority received by FMCSA is being processed as though there were no changes in the law.

At this early stage, it is not clear how the marketplace will respond to the change in registration requirements. So long as FMCSA continues to process applications, registrations can continue. If shippers decide that, as a matter of due diligence in their purchasing practices, they will do business only with registered brokers and forwarders in good standing with FMCSA, then a prospective broker or forwarder will have to respond accordingly even if there is no legal requirement.

At some point, FMCSA will have to address how they want to treat brokers and carriers. The word inside the Beltway is that FMCSA would like to get out of the registration business so that it can focus its resources on matters more directly related to safety.

For more information on this topic, contact Bob Spira at rspira@bfca.com or 216.363.4413.

[1] The new language applicable to general freight property brokers and freight forwarders contrasts clearly with the new requirements for household goods brokers and freight forwarders. The household goods industry is moving into a new era of consumer protection regulation by FMCSA.

[2] Although the regulations above have not been rescinded by FMCSA, they are no longer enforceable by FMCSA. Recent examples of the effect of deregulating legislation illustrate the point. When regulatory requirements are repealed by Congress, reduction in jurisdiction is selfenforcing. Thus, for example, when Congress relieved motor carriers of the need to file tariffs by the enactment of the Trucking Industry Regulatory Reform Act of 1994, the ICC simply stopped accepting tendered tariffs, notwithstanding that the regulations continued to require their filing.

Freight Charges v. Freight Claims: The Set-Off Controversy

Shippers, intermediaries, and motor carriers often find themselves facing the issue of whether or not a shipper's alleged freight claim can be set off against a motor carrier's claimed freight charges. In other words, can a shipper refuse to pay a $5,000 freight bill if the carrier is theoretically liable for freight damage in excess of $5,000? Some shippers view such a right as an essential business tool. Some carriers view such a right as an entirely illegitimate and unfair bargaining tool.

Contrary to the perception of many in the industry, no federal law or regulation currently governs this theoretical right. Rather, the right of set-off is purely a creature of contract or state common law. As a result, shippers, brokers, and carriers should specifically address this right in their transportation contracts one way or the other. In deciding whether and how to address a right of set-off in a transportation contract, the parties should give careful consideration to the following practical issues, among others.

1. *Cash Flow*

The right of set-off can dramatically affect the parties' cash flow. This is particularly true when the carrier in question is on the smaller side or sells its accounts to a factoring company. For instance, most factoring companies require the carrier to warrant or otherwise promise that the assigned accounts are not subject to a right of set-off. If the carrier breaches that warranty or promise, the factoring company may be granted significant rights against the shipper or broker under its factoring agreement. Therefore, the parties should carefully consider the extent to which exercising a right of set-off may affect the parties' cash flow and, accordingly, their respective bargaining power.

2. *Cargo Insurance*

Cargo insurance can influence the manner in which set-offs are negotiated.

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On the one hand, many shippers are acutely aware that carriers' cargo insurance policies are often riddled with exceptions and exclusions that substantially limit the ultimate recovery. As a result, shippers rightly recognize that exercising a right of set-off, whether authorized by contract or not, may give them an upper hand in negotiating a resolution to their freight claim. Due to the cash flow considerations mentioned above, a carrier may feel pressure to resolve a cargo claim even though it may do so without giving its cargo insurer adequate notice or the requisite role in claims handling. On the other hand, the carrier's certificate of insurance required by FMCSA means that the carrier has obtained a BMC-32 endorsement to its motor carrier cargo liability policy. This endorsement already gives shippers some limited comfort, at least with respect to very modest claims (under $5,000). However, the obligation to obtain the endorsement may apply only to common carriers. FMCSA is proposing to eliminate it entirely for all carriers of general freight. In any event, the parties should give real consideration to the role of the cargo insurer in resolving freight claims.

3. *The Loss of Freight Charge Discounts*

A shipper or third-party logistics provider may find that setting off even a perfectly valid freight claim against a carrier's freight charges results in the loss of a significant freight charge discount. For instance, a carrier's tariff might state that billed freight charges are based on a discounted rate that will be lost or compromised if payment is not made within a certain number of days. In other words, a shipper or broker who is owed only $5,000 in freight charges shortly after the delivery of the damaged goods may find that the freight bill increases to $7,500 if payment is not made within 60 days, regardless of the reason for non-payment or the fact that the parties are negotiating a resolution to a valid freight claim. Therefore, the right of set-off negotiated between the parties should ensure that the parties fully understand what consequences may follow from exercising the right of set-off.

4. *Attorneys' Fees*

Just as a carrier may be entitled to withdraw freight charge discounts when presented with a freight charge set-off, a carrier may include a provision in its contract or incorporated tariff that awards the carrier attorneys' fees incurred in collecting freight charges. As the shipper or third-party logistics provider will inevitably bring a counterclaim for its freight claim, the carrier may be in the unusual position of being able to recover from the shipper the attorneys' fees associated with the defense of its freight claim (assuming for the moment that the insurer is not providing the cost of defense already). The extent to which a carrier can actually recover its attorneys' fees under these circumstances varies from state to state. Shippers may also include provisions relating to the recovery of attorneys' fees in connection with freight claims, although the same state-specific limitations apply.

In summary, shippers, third-party logistics providers, and carriers are all well-served by confronting the possibility of setting off freight charges with a freight claim and memorializing the agreement struck in sufficient detail in the governing transportation contract. The parties should not have any doubts whether the right to set-off has been prohibited or permitted by the contract.

For additional information on this topic, contact Marc Blubaugh at mblubaugh@bfca.com or 614.223.9382.

Conduct Due Diligence before Hiring a Motor Carrier

What is appropriate "due diligence" for a shipper who needs to hire a motor carrier? Before tendering any freight to a carrier, a shipper should:

1. Ask the carrier for a copy of the carrier's operating authority and certificates of liability and cargo insurance. An additional insured endorsement on the liability policy would be ideal, but may not be available.

2. Check the Federal Motor Carrier Safety Administration's "Safersys" on-line database for information about the carrier (www.safer.fmcsa.dot.gov).

   – Under "Company Snapshot," Safersys provides general information about the carrier including number of vehicles, number of drivers and types of cargo carried.

   – Under "Licensing and Insurance," Safersys confirms that the carrier is registered and has required evidence of insurance on file. Most carriers are required to have only $750,000 of liability insurance. Carriers hauling hazardous materials are required to have up to $5 million of insurance coverage.

   – Under "SafeStat," a shipper can research the safety performance history of a carrier including any accident

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record and safety rating issued by FMCSA. Depending on the results of an FMCSA audit, FMCSA will issue a rating of "satisfactory," "conditional," or "unsatisfactory." Some shippers have established policies under which they can hire only carriers with a "satisfactory" safety rating. The problem with such a policy is that it excludes carriers who have no safety rating. A shipper should not necessarily be concerned if a carrier has no safety rating. Thousands of carriers have no rating because they have not been audited by FMCSA. A carrier with a "conditional" rating may or may not have serious safety compliance problems. A shipper should try to find out more before using the carrier. A carrier with an "unsatisfactory" rating has significant compliance issues with FMCSA. The carrier will not be in business for very long if the deficiencies are not corrected. The regulations give the carrier a limited period of time to get its act together. Although it is a valuable tool for evaluating prospective trucking service providers, FMCSA strongly cautions shippers not to rely exclusively on SafeStat for safety performance data. Unfortunately, the SafeStat database has some flaws, and has even included inaccurate information about some carriers.

Shippers need to be sure that they know as much as possible about the carriers to whom they are tendering freight. There is much to be learned from information about motor carriers made available to the public by FMCSA.

For more information on this topic, contact Bob Spira at rspira@bfca.com or 216.363.4413.

On The Horizon

Benesch's Transportation and Logistics Conference

December 1, 2005
The City Club of Cleveland

The theme of this year's conference is "Maximizing Opportunities and Minimizing Risks in Transportation and Logistics: How the Law can Help."

For further information and registration, please contact Megan Thomas at 216.363.4174 or mthomas@bfca.com.

Transportation Lawyers Annual Conference

May 2006
Orlando, Florida

Marc Blubaugh will be moderating a panel discussion on "The 3PL Revealed: A Riddle Wrapped in a Mystery Inside an Enigma."

Recently Published

Contact us for reprints of any of the following:

When the Act of a Government Constitutes a Valid Defense to a Freight Claim
Marc S. Blubaugh
Transportation Lawyers Association
October 2005

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Eric L. Zalud
CCH Federal Carriers Reports
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Select the Right Freight Carrier
Robert M. Spira
Paperboard Packaging
September 1, 2005

Secure a Competitive Edge in Transportation Contracts
Marc S. Blubaugh
Columbus Business First
August 8, 2005

Forcing Yourself to Understand 'Force Majeure'
Marc S. Blubaugh
The Informer (American Trucking Association)
March 2005

Not All 3PL's are Viewed Same Under Rule of Law
Marc S. Blubaugh
Columbus Business First
February 11, 2005

Turning Lemons into Lemonade: Effective Tactical Handling of Driver Logs
Eric L. Zalud
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February 2005

Recent Presentations

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Robert M. Spira
Eric L. Zalud
Transportation Intermediaries Association
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June 8, 2005

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Marc S. Blubaugh
Council of Supply Chain Management Professionals
March 17, 2005

Freight Claims: What The Courts Had To Say in 2004
Marc S. Blubaugh
Delta Nu Alpha
March 2, 2005

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