

Logistics and the Law Double Trouble

Logistics Management

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The gradual deregulation of all four modes of carriage during the past 28 years has had a significant impact on shippers' transportation costs and operating strategies. Nevertheless, legal and regulatory issues continue to challenge logistics managers, largely because the law is rarely taught in transportation and logistics courses.

Yet transportation law and regulatory matters are still important, as logistics managers are the ones who get blamed when a shipper is sued for unanticipated freight charges. The undercharge fiasco of the '80s and '90s as well as the problems with bankrupt freight-payment companies bear testimony to this statement.

The consequences of such ignorance are costly. That's why shippers should give serious consideration to two recent developments: 1) The U.S. Department of Transportation's attempts to rid itself of its responsibilities for protecting the shipping public; and 2) The decision in *Schramm v. Foster* exposing shippers and third parties to being sued for negligently hiring truckers.

FMCSA Proposals Hurt Shippers

The U.S. Department of Transportation (DOT) and its Federal Motor Carrier Safety Administration (FMCSA) took several actions last year that reveal a concerted effort to free themselves from responsibility for everything but motor carrier safety and security. (For a look at how the FMCSA views its mission, see Page 36 .)

First came a proposed rulemaking to eliminate all cargo insurance requirements for motor carriers and surface freight forwarders. The FMCSA's justification for this revolutionary proposal was that "These carriers typically have insurance well above the FMCSA limits [\$5,000] because their shipper clients generally require it as a condition of doing business."

This statement reflects a lack of understanding of the real value of the **BMC-32 Endorsement**, the provision that makes deductibles and exclusions a nullity in a trucker's policy for the first \$5,000, or for the first \$10,000 of a multiple-vehicle accident.

Virtually every cargo policy ever issued to a motor carrier contains numerous exclusions from liability, such as theft from an unattended vehicle, an unattached vehicle, or a dropped trailer; employee infidelity; or losses due to a fraudulent scheme. Many policies contain exclusions for high-risk commodities such as electronics, prescription drugs, and tobacco. Shippers rarely are told of these exclusions by a carrier's salesperson or management until a loss

occurs. Unsophisticated shippers naively believe that if they have a Certificate of Insurance on file for a carrier, they will be paid for any claim that occurs in transit. Due to the presence of deductibles and exclusions, however, in practice insurance covers the carrier for everything except what happens to cause the loss!

Thanks to the existence of the BMC-32 Endorsement, claimants have been able to recover many millions of dollars in transit losses directly from the insurers, rather than chase carriers for these losses in the courts. It is the best legislation and government regulation ever enacted to protect the shipping public, but now the DOT and the FMCSA propose to eliminate it.

Nothing has changed to make this protection unnecessary. Then why is the FMCSA trying to get rid of it? The answer, in this writer's opinion, is that the proponents of this ill-conceived proposal do not understand the regulation or its application in the real world. It is not the \$5,000 per-vehicle coverage that is important; it is the fact that claimants can recover up to \$5,000 for losses that would otherwise be excluded or deducted from the policy.

It has been this writer's experience that cargo insurers often improperly deny coverage on these small claims in violation of the terms in the BMC-32 Endorsement, knowing that the cost of litigating them will discourage claimants' pursuit in the courts. It is for that reason that the Freight Transportation Consultants Association (FTCA) has suggested enactment of "self-help" legislation governing actions against insurers. The proposal is similar to 49 U.S.C. § 14704, a statute that enables any person who has been damaged by a motor carrier, freight forwarder, or broker as a result of their violation of any provision of the Interstate Commerce Act, or a regulation promulgated thereunder, to sue in the federal courts and recover their attorney fees as a cost of the action.

By making insurers liable for damages and attorneys' fees, the proposed legislation would remove the cost factor that discourages shippers from litigating small claims, while also relieving the federal government of the cost of enforcing this regulation.

In addition, the FTCA argued that the FMCSA needs to promulgate regulations to modify insurers' Certificates of Insurance by adding the exclusions in the policies, which currently are not shown. Without knowledge of the exclusions, holders of Certificates of Insurance don't know whether or not their freight would be covered for the most frequent causes of transit losses.

The FTCA further requested that **Certificates of Insurance** be amended to make insurers legally liable for failing to notify certificate holders of any modification to or cancellation of coverage. The present form merely states that the insurer will "endeavor" to notify the holder, but that it will have no liability if it should fail to do so.

A second action taken by the DOT and FMCSA that is adverse to the shipping public occurred when the agencies surreptitiously had a change in the DOT Secretary's authority over brokers and freight forwarders inserted into SAFETEA-LU, the highway funding bill signed August 20, 2005. The change consisted of substituting the word "may" for "shall" in the statute that delegates to the Secretary authority to regulate these intermediaries.

There is no consensus as to whether the Secretary must initiate a rulemaking to determine whether continued regulation is needed to protect the public, or whether this change has been accomplished effective August 20, 2005. In either event, the elimination of regulation of brokers and freight forwarders could have a devastating effect on the shipping community and could set back the advances made by the intermediary industry since 1980, when entry controls were relaxed. Continued regulation will help to rid the industry of dishonest, unstable entities, while eliminating regulation will attract more dishonest operators.

The Schramm Decision

As if shippers, brokers, and third-party logistics companies (3PLs) did not have enough problems with truck and driver shortages today, a federal district court in Maryland has compounded these and other problems inherent in hiring truckers. The court has refused to dismiss a Motion for Summary Judgment against a broker/3PL, sending the case to a jury to determine whether or not the broker was negligent in hiring the trucker that caused an accident that seriously injured two young men.

The crux of the court's decision was that "an employer may be held liable for negligence in selecting, instructing, or supervising [an independent] contractor." The court ruled that although the broker/3PL was not the carrier under federal law, "its self-proclaimed status as a 'third-party logistics company' providing 'one point of contact' service to its shipper clients is sufficient under Maryland law to require it to use reasonable care in selecting the trucker whom it maintains in its stable of carriers."

This decision will be used by plaintiffs to attempt to hold any entity that hires truckers responsible for any damages, injuries, or loss of life resulting from the truckers' operations. The question now is, what constitutes "reasonable care" when selecting a trucker in today's business environment?

The court's standard for selecting carriers, in this writer's opinion, is completely unrealistic and unattainable. That standard included "the subsidiary duties (1) to check the safety statistics and evaluations of the carriers with whom it contracts, available on the SafeStat database maintained by FMCSA, and (2) to maintain internal records of the persons with whom it contracts to assure that they are not manipulating their business practices in order to avoid unsatisfactory SafeStat ratings."

The court concluded that "these obligations are not onerous." Shippers, brokers, and 3PLs, however, disagree with the court's conclusion. It is the



FMCSA's duty to check the safety of the carriers it registers for interstate transportation.

When hiring trucks, time does not permit delving into each carrier's database to determine how many accidents it had in the past, how many trucks and drivers have been taken out of service, the carrier's **SafeStat score**, and more. (A DOT score above 75 is not acceptable; the carrier in Schramm had a score of 74.) It should be sufficient to check a carrier's record the first time it is used and then recheck it periodically to be certain that it continues to maintain a "satisfactory" rating.

Many truckers have not been rated by the FMCSA but brokers need to hire them nonetheless. Yet this court ruled that "? it seems entirely reasonable to require firms, including third-party logistics companies, who assist newcomers with market entry, to evaluate carriers' safety-control measures in the absence of a DOT rating."

The broker/3PL in this case presented evidence that it deals only with carriers that have "full insurance coverage," verifies that coverage, and keeps a copy of documents that prove the carrier has Federal Operating Authority and a current insurance certificate with a minimum of \$750,000 auto liability coverage. The company also testified that it regularly checks with carriers to make sure their coverage is current and has been renewed at necessary intervals.

This is a good procedure to follow, but how often must one check a carrier before hiring? If the hiring party did not check on the date it was hired but instead relied upon year-old information, plaintiff's argument will certainly allege negligence in not performing a more current inquiry of the carrier's safety status. It will be a no-win situation for any party that hires trucks.

Accordingly, the best preventive measures that shippers, brokers, and 3PLs can take when hiring a motor carrier include:

Reviewing and strengthening procedures for hiring carriers, to the fullest extent possible.

Insisting upon staff's strict compliance with these new procedures.

Using private services that update information when there are changes in carriers' insurance and licensing.

Conducting an independent investigation of carriers that do not have a DOT safety rating.

In light of this court decision, brokers and 3PLs would be wise to review contracts, bills of lading, documentation, and sales and marketing materials to be certain that it is clear to existing and potential customers that they are not carriers.

These entities have exposed themselves to allegations that they are operating as carriers by changing their corporate names to include the word "Logistics," permitting their name to be shown on documents as the carrier, paying loss and damage claims, and purchasing cargo insurance policies.

There are legally correct ways to operate as an intermediary without being exposed to potentially devastating lawsuits. Shippers that hire intermediaries will want to be cognizant of how the Schramm decision could affect their service providers while at the same time making sure that they, too, will not be harmed as a result.

What is the FMCSA's Mission? Jeff Berman The Federal Motor Carrier Safety Administration (FMCSA) was created as an independent agency within the U.S. Department of Transportation in 2000, in accordance with the Motor Carrier Safety Improvement Act of 1999.

Some of the statutes overseen by the FMCSA have a direct impact on shippers, but shippers' needs don't appear to be high on the agency's priority list. According to its website, the FMCSA's mission is to "reduce crashes, injuries, and fatalities involving large trucks and buses."

The agency says its chief objectives include: drafting and carrying out data-supported regulations that balance motor carrier safety and industry efficiency; employing information systems that are designed to enforce safety regulations; and establishing partnerships with federal, state, and local agencies, the motor carrier industry, and safety groups, among others.