

Parcel Carrier Service Guarantees

Keep Your Carriers Accountable – Retain Your Rights

Parcel carriers provide a wide selection of premium services. These services typically come at an equally premium price. To reinforce the value of these services, carriers offer service guarantees. Typically guarantees involve refunding transportation charges (not accessorial or surcharges) for packages that are not delivered within established time limits.

Carrier Perspective

The parcel carriers have been backing away from service guarantees for the past several years. For example, in October 2008 UPS announced that they would no longer refund fuel surcharges for Guaranteed Service claims. Also, in 2009 UPS increased the time period around the holidays for which Ground Service Guarantees do not apply. In previous years Service Guarantees were suspended for 14 days prior to Christmas. In 2009 this exception period was extended to include December 1 through December 31. While UPS is used for these examples, FedEx is also backing away from service guarantees. While the carriers have always tried to negotiate away GSR rights, new approaches have crept in and are having an effect. Carriers seek to limit their exposure to service guarantees in three ways. The first is to

maintain high service levels. Although the carriers do not typically publish their on-time delivery levels, in discussions carriers typically claim adherence to guaranteed service level percentages in the high 90s. In fact their service adherence is typically very high. However, service varies from carrier to carrier and from account to account. While some shippers may experience service levels of 99% or more, others experience substantially lower on-time delivery percentages, some as low as the mid eighties.

These guarantees are also subject to varying terms and limitations, which have become more stringent as time has gone by. The fact that carriers continue to place increased restrictions and exceptions on service guarantee refunds demonstrates that it is an issue to the carriers, and further demonstrates their reluctance to refund hard-earned



revenues. Some of these exceptions are reasonable (incorrect address provided, shipments scheduled for delivery on a holiday, etc.). Others are dubious at best. For instance,

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carriers require that you file for refunds within 15 days of the scheduled delivery date. However, depending on the timing of the invoice and the pickup date, as many as seven days may have elapsed by the time you have what you need, and are in a position to take action and file a claim.

FedEx will also deny a service refund if a package is originally coded as commercial delivery, but is later re-classified residential. The entire list of restrictions varies by carrier, but they are extensive and severely limit the instances in which a service guarantee claim will be honored.

Finally, carriers seek to remove service guarantee rights contractually. If you have re-negotiated your carrier pricing agreements in the past several years you may have

noticed a clause which waives your right to file service guarantee claims. Carriers attempt to negotiate these rights away whenever possible, particularly for large, high dollar shippers. Negotiation strategies vary in these cases. Sometimes the guarantee waiver is not discussed and the fact that you are waiving your rights is overlooked in the agreement's numerous terms and conditions. Other times a "buy out" is offered, where carriers offer an additional discount in exchange for the waiver. This is somewhat misleading. First, the level of discount offered is usually 1% or less. This is well below the carriers' pain threshold within the negotiation; meaning that the additional discounts could likely be included with or without waiving the GSRs if the agreement was strongly negotiated. Also, the additional discount is usually set lower than the shipper's GSR history. For example, if a shipper files for and receives refunds of \$50k annually, the additional discount offset will usually be less than this figure. Carriers will assert that the personnel and administrative costs you incur filing your

claims offset the delta. However, as will be discussed below, this too is misleading. Finally, carriers may indicate that the only way they have been able to offer whatever discounts they have is to waive service refunds, and that removing the waiver would require reducing discounts. If you made service refunds a condition of your Request for Quote (RFQ) process, overcoming this objection should be relatively simple.

An example is probably in order and will provide a clearer understanding of the points covered. These numbers are for illustrative purposes only.

SUN	MON	TUE	WED	THU	FRI	SAT
	1 Scheduled Delivery Date	2	3	4	5	6 Invoice Date
7	8 First Available Processing Date	9	10	11	12	13
14	15 Claims Filing Deadline	16	17	18	19	20

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Figure 1: Filing Timeline

Company X pays \$5 million dollars annually in gross (before discount) parcel cost. In the past 12 months Company X filed for \$200k in GSR claims. Due to the carrier's GSR restrictions, however, only \$100k of those claims were honored and paid. The assumption then would be that the carrier would need to increase the discount by 2%. But, let's look at a few factors that make this a faulty assumption.

- A 2% discount increase does not necessarily equate to a 2% net cost reduction. Factors like minimum package charges, accessorials and surcharges, and DIM rating (among others) reduce the impact of increased incentives. While the factor will vary from shipper to shipper, a 2% discount increase could impact net cost by 1.5% or less.
- While Company X is currently being approved for \$100k in GSR claims annually, this does not necessarily mean that \$100k is all that is available. By filing in a timely manner and by making use of sophisticated systems a third party auditing firm may be able to achieve a much higher pay rate. Based on the experiences of one auditing firm it is not unusual to double the GSR recovery rate relative to the GSR recovery when claims are filed internally.
- We discussed earlier the carriers' perspective on administrative costs and their impact on GSR offset discounts. Again, the most typical

administrative factor is 50%. So, in the case of Company X the carrier's goal is to offer an unqualified discount increase of only 1.0%.

Accountability

There is a certain balance of power in the carrier/shipper relationship. You have the power to move your business from one carrier to another. Moving your business is a pretty big stick to wield in negotiations. On the other side of the equation the carriers have your

agreement, which they absolutely understand better than you. They also have hundreds of pages of service guides and tariffs which explain, and in many cases eliminate, your rights. At the end of the day, service guarantee refunds may be the thumb on the scale - the only thing that tips the balance of power in the shipper's favor. Carriers provide service guarantees to show and instill faith in their services. Service Guarantee Refunds are the sole tool you have at your disposal, short of moving your business, to hold the carriers accountable for their service. You insist on accountability in your own organization. Why should you require less from your vendors? Parcel carriers are a critical part of your supply chain and in many cases serve as an early driver of customer satisfaction. If your service levels are not being met you must have a mechanism to drive change.

There is an inherent problem when carriers offer to "offset" GSR waivers with increased incentives. Typically carriers begin the calculation of the offset by looking at historical claims paid. However, GSR claims paid only serves as the baseline. This number is then reduced under the auspices of administrative costs. Carriers typically apply what I call an "Administrative Cost Tax" when determining the discount offset they will offer for a GSR

(\$100k in historical claims paid x the admin cost factor of 50% / \$5M gross spend)

Carrier Calculation

Annual Gross Spend	\$5,000,000
Historical Claims paid	\$100k
Administrative cost factor	\$50k
Offset required	\$50k
Nominal discount increase required	1.0%
Accessorial/Surcharge/ etc. compensation	0.0%
Total nominal discount increase	1.0%
\$\$\$ Impact of offset	\$50k

Logical Calculation

Annual Gross Spend	\$5,000,000
Assumed auditing firm claims paid	\$200k ¹
Administrative cost factor	\$0
Offset Required	\$200k
Nominal discount increase required	4.0%
Accessorial/Surcharge/ etc. compensation	1.0% ¹
Total nominal discount increase	5.0%
\$\$\$ Impact of offset	\$250k

¹ Varies from shipper to shipper

buyout. They will claim that the shipper incurs high administrative costs in filing for GSR claims. The most commonly used percentage is 50%. Using this logic the carrier is likely to offer discounts that will (supposedly) offset only 50% of the historical claims paid. What the carrier is trying to say is that because you incur administrative costs in filing claims, you are not entitled to an offset of the full claims value. This is faulty logic, because the reverse is also true. The carrier also incurs costs in handling your GSR claims. By the carrier logic you must 'pay' for your administrative cost savings with a lower discount. The carrier, however, would receive their administrative costs savings for free. A much more logical scenario would be that both the shipper and the carrier receive the administrative cost savings for free (call it a wash) and the focus of any proposed offset focuses on the value of the claims only.

Conclusion

So, does this mean companies should throw in the towel on guaranteed service? On the contrary, we believe guaranteed service is more important than ever. The only reason the carriers would be making such an issue of

Seize the Opportunity:

Many shippers fail to take advantage of carrier service guarantees. As described above, carriers do not make it easy to file for and receive credit for service failures. Maximizing the service guarantee refunds to which you are entitled requires resources, experience, and systems that most shippers simply do not have. Although you may not be realizing significant savings at present, there may well be significant opportunities for savings if sophisticated, cost-effective methodologies are employed. Use of a third party with experience in recouping service guarantee monies could present you with substantial savings.

guaranteed service is if they expect it to be a larger issue going forward. With falling yields and tighter margins the carriers have less money to invest in their networks. The result may well be a reduced ability to maintain service levels.

However, you are still paying for that service level. To paraphrase Dylan Thomas, "Rage against the dying of guaranteed service." You're still paying for it. The carriers should provide it. More importantly, they should be held accountable for providing it.

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