

**OCEAN SHIPPING REFORM ACT OF 1998
OVERHAULS TRANSPORTATION SYSTEM
FOR U.S. EXPORTS AND IMPORTS**

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Congress recently passed and the President signed the Ocean Shipping Reform Act of 1998, which modernizes and deregulates the international ocean shipping business. The long-awaited Reform Act sets in motion a transformation of our common carriage system — in which all pricing is filed with the government and made public — into a contract-based system in which pricing will be confidential. The revamped structure presents challenges and opportunities for companies of all sizes that import or export goods by sea, and for a myriad of shippers' associations, ocean and inland carriers, freight forwarders and consolidators, ports, terminal operators, traders, brokers, distributors and logistics managers. However, the reforms create potential pitfalls for those who fail to take a fresh look at a fast-changing commercial landscape and to redirect their strategy.

The Reform Act takes effect May 1, 1999, but changes are already occurring. This paper summarizes the elements of reform, as enacted, and identifies potential opportunities.

Major Changes. The Reform Act amends the Shipping Act of 1984 and other pertinent laws to reconfigure U.S. regulatory ground rules as well as the commercial playing field.

- **Confidential contracts:** Nearly all ocean freight exported from or imported into the United States will soon be shipped through privately negotiated contracts in which rates, charges, discounts and other pricing terms will be confidential — in line with other world trades where transportation cost is not a matter of public record. Confidentiality is not *required* under the Reform Act, but will prevail simply because it is commercially available. Most contracts will be filed with a government agency, the Federal Maritime Commission (FMC), for monitoring purposes, although only a few contract terms, unrelated to pricing, will be made public.
- **Contracting flexibility:** Contracts may be negotiated between one or more shippers, on one hand, and on the other, a single carrier or multi-carrier group. Significantly, for the first time, any carrier that belongs to a group authorized to jointly set prices

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has complete freedom to individually negotiate private contracts with shippers, independently of other carriers in its group. Shippers may enhance contracting leverage by participating in non-profit shippers' associations. Contracts may cover freight shipped in single or multiple trade lanes or may extend globally.

- **Diminished role of tariffs:** A small portion of ocean freight *not* covered by confidential contracts will move pursuant to tariffs or price lists which will no longer be filed with the FMC but will be readily accessed by the public, probably via the Internet. The freight volume moving under such tariffs is expected to soon become minimal. The disappearance of mandated "official" tariffs opens a wide range of contractual service prospects that did not exist under the 82-year-old filed rate regimen.
- **Reduced enforcement tools:** Protection against undue discrimination will be reduced, but the FMC will continue as an independent agency empowered to address unreasonable or harmful practices, especially as they may affect smaller shippers and U.S. ports. The Reform Act eliminates "me too" (equal access) contracting and virtually negates a former "similarly situated shipper" anti-discrimination standard. Private contracts are governed largely by contract law, the courts and related dispute resolution processes.
- **Common carriage redefined:** Common carriage principles are retained more in form than substance, as they are neutralized by a system featuring private contracts. For example, the so-called "filed rate doctrine," involving strict adherence to government-filed tariffs, will no longer apply.

Commercial Opportunity. Businesses should prepare now for the reformed system. Professional and trade organizations are scheduling educational seminars about the Reform Act and its perceived effects. The trade press contains countless articles and analyses of the legislation. However, a specific approach that is appropriate for a particular company will depend on a variety of facts and circumstances, commercial and legal. These factors should be evaluated carefully and an action plan should be developed. Generic approaches are only a starting point.

- **Shippers** should critically examine the transportation service providers utilized for their shipments, consider potential service options and develop their strategic objectives and priorities, including any customized requirements. Short- and long-term considerations must be addressed. Prior to negotiating contracts with carriers, shippers should prepare detailed contract clauses and provisions to meet their requirements, if not a complete draft of the proposed contract; shippers

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should avoid relying on a standard format or boilerplate produced by the carrier. Shippers that have not joined shippers' associations should consider the advantages and limitations of doing so. Under the Reform Act, not only is pricing confidential, so are a shipper's (or association's) identity, a carrier's service commitments and any inland service points. It should be assumed that carrier mergers, buyouts and alliances will continue to alter shippers' range of choices. In view of reduced information about competitors' transport costs available in a deregulated environment, consultant services may be in demand to develop such information.

- **Ocean carriers** belong to various groups that enjoy antitrust immunity and are monitored by the FMC. Some groups are considering new structures in response to Reform Act changes. It appears unlikely that traditional freight conferences (*i.e.*, price-fixing groups) will exist as such for long. Carrier operating alliances and so-called policy "discussion" groups may well emerge as the centers of future cooperation among carriers, the former to achieve cost savings and the latter in an effort to develop general pricing guidelines consistent with contract confidentiality. A key to carriers' post-reform success may be in market-driven initiatives by carriers, individually and with their alliance partners, to build relationships with vendors and customers.
- **Transportation intermediaries** include ocean freight forwarders who book ship space and provide incidental services to shippers, and so-called NVOCCs, *i.e.*, ship space resellers who purchase space in volume from ocean carriers and resell it to shippers at a profit. The Reform Act does not permit NVOCCs to enter contracts with shippers, so they must resell space pursuant to publicly available price lists. NVOCCs, however, may enter into private contracts with ocean carriers in purchasing space, and many NVOCCs have begun to consolidate and/or band together in shippers' associations to improve their bargaining position for wholesale rates. Meanwhile, many freight forwarders are merging with NVOCCs, or are themselves becoming NVOCCs, in pursuit of strategic goals.
- **Inland carriers** are rail and truck lines that provide connecting services between port terminals and interior (overland) locations. The Reform Act permits two or more ocean carriers to jointly negotiate (subject to antitrust laws) with an inland carrier regarding rates for overland services, ranging from local drayage to container stack-trains. Some ocean carriers are reportedly considering withdrawal from large-scale intermodal operations in order to focus on their core port-to-port business. In any event, the Reform Act is likely to change relationships among ocean carriers, rail and truck lines, and shippers.

- **Ports, terminal operators and other entities** are competing vigorously to maintain viability as players in a more concentrated international marketplace. As ocean carriers merge and combine, ports and local facilities are faced with fewer prospects to build their business base. Entities of many descriptions are linked in an international chain of transport services and are impacted directly or indirectly by the Reform Act.

Regulatory Implementation. The FMC has commenced rulemaking proceedings, and is soliciting input from interested persons on how best to implement the Reform Act. The FMC is under a tight deadline because the Act mandates that final regulations be prescribed by March 1, 1999 — 60 days before the Reform Act becomes effective. Interested parties must react promptly to be heard.

Future. Each person's or company's action plan addressing Reform Act strategy should be treated as a working paper. As with other transportation modes following deregulation, developments are ongoing, change is dynamic and further review is essential.

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