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Ocean Carrier Bid Season – 2024 Edition

Client Bulletins

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Yet again the ocean freight bid season is unfolding against a backdrop of uncertainty. The 2024 season brings a confluence of economic, geopolitical, trade, and industry-related issues that have created a complex environment for shippers, NVOs, and carriers alike.

We all have fresh memories of COVID-19 port congestion, ongoing disruptions and diversions due to the Russia-Ukraine conflict, and the more recent instability in the Middle East and Red Sea. Concerns about route disruptions, vessel availability, labor disputes, election cycles, trade imbalances, new environmental compliance obligations, and the FMC's regulatory changes arising out of the Ocean Shipping Reform Act of 2022 (OSRA 2022) have only added to the complexity that will impact future ocean freight negotiations.

Stakeholders on all sides have a few guiding principles in this environment that can help in managing operational and commercial risk—ideally in pragmatic fashion. We explore some of those principles that we are seeing from a few different angles: (1) rates and charges, (2) inland services, (3) service failures, (4) sanctions and global compliance, and (5) extracontractual terms.

Rates and Charges – Realism About Vessel Capacity, Container Capacity, Shipping Lanes, and Disruption

The first step in operational planning is always some level of forecast for future needs. The added challenge in this market is that sourcing origins and routes may need to be realistically flexible, which can mean greater realized rate variance. As best as is possible, all purchasers of capacity are looking to achieve service-level visibility and cost-related predictability.

Current factors driving rates higher include diversion and capacity constraints, strong demand with increased volumes, an earlier-than-usual start to peak season, and operational disruptions at ports and terminals. Diversions and rerouting vessels to avoid lanes in zones of conflict in the Middle East and Red Sea have led to increased base rates due to longer transit times, higher fuel and labor costs, increased war risk premiums, and container availability issues. The compounding effect of the demurrage, detention, and dwell charges (collectively, D&D Charges) arising out of operational issues and equipment shortages have significantly increased the overall cost of ocean freight in recent years. Despite that OSRA 2022 and the FMC's related regulations sought to mitigate unfair D&D Charges imposed on shippers by ocean carriers and marine terminal operators, the impact of these efforts remains to be seen.

Inland Services – Surface Traffic and Container Management Under Review at Origin

Attention to inland services has grown in recent years, and it continues today, particularly for origin services in the People's Republic of China. Those activities can include outbound consolidation of container loads, container pooling and management, and forwarding and NVO services, as well as coordination with inland US providers, such as customs brokers and dray operators.

Doing so allows for greater focus on those inland activities in the interest of better visibility and management of cargoes. As a strategy, this approach to inland services is reminiscent to the fragmentation of inland US services that many shippers embarked upon in the early years of COVID-19. Many large global service providers are available to offer comprehensive “control tower” or 4PL services under contract with hopes of greater performance at origin. More localized services are also available. The service delivery may be a technological solution, an asset-light solution such as offering an available container pool, or a comprehensive end-to-end solution with in-sourced or third-party dray and ocean carriage. A best practice we have observed is to balance complexity against efficacy. Testing services in a market under a durable contractual foundation can allow for alignment of expectations and proof of concept before signing up for global origin services.

Service Failures – Production or Inventory Scheduling May Be Less Precise

Inbound cargoes to the country of consumption or distribution are the first acute casualty of service disruption. One point we have noticed across the supply chain is the growth across cargo owners and carriers alike in working together to better communicate on needs, services, and reporting. This is positive because it opens the door to a net effect of collaboration, its impact on operational planning, and the possibility for dynamic models accommodating service and cost.

The need to work together on throughput is not without cause. Anecdotally many have seen a recent uptick in service failures, including rolled cargo, blank sailings, and diversions, that have helped carriers manage capacity on the one hand but have caused supply chain disruptions and delays on the other. Overbookings and capacity constraints have been the leading causes for rolled cargo, while blank sailings and diversions are reducing available vessel and lane capacity that creates supply shortages to increase freight rate volatility and additional transportation costs. Stakeholders can look to avoid or mitigate the impact of service-level failures by negotiating flexible forecasting terms, an achievable MQC cadence, liquidated damages, dead freight, and escalatory procedures for addressing repeat occurrences of service failures.

Sanctions and Global Compliance – Moving Product Internationally While Staying Out of the Headlines

Trade compliance is an area where risk-appropriate approaches are desirable. There is no off-the-shelf compliance program suitable for every company in every segment of the supply chain. Even so, best practices and high-impact risks do exist that merit consideration by enterprises large and small.

This global shipping environment brings its own unique challenges. It is important to maintain awareness and suitable compliance tools across operations teams. War in the Middle East has elevated the risk of noncompliance with anti-boycott rules. A request from any shipper or its suppliers, or third-party service providers, to boycott a certain country or its companies (e.g. Israel flagged vessels) may be violative and could draw penalties. War in Europe has elevated the risk of noncompliance with economic sanctions. The tangible impact could involve inability to move certain items across the European theater, or transfer funds for the same, but it could even extend to certain ocean carriers that trade with adversaries of the United States (e.g. Russia) requiring contract edits that are typically non-negotiable. Even the longstanding rise of tensions with the People’s Republic of China can drive risk. Knowingly carrying, forwarding, or otherwise facilitating semiconductor trade with China is a real possibly today and may well yield a violation of General Prohibition 10 under the Export Administration Regulations. Less dramatic compliance concerns are also appearing in service contracts. The rollout of ocean carrier emissions requirements across Europe has been an increasing point of negotiation as shippers and carriers balance the cost of compliance.

Extracontractual Terms – Remember that Out of Sight is NOT Out of Mind

Every transportation procurement lead, operations manager, and in-house counsel desire certainty of terms as best as possible. In the years since COVID-19, carriers have increasingly pushed to incorporate their own extracontractual terms, such as their tariffs and bill of lading terms and conditions (Carrier Terms), into ocean contracts. If this is done well it can have the effect of certainty rather than merely incorporating extracontractual terms.

The reasons for clearly spelling out Carrier Terms, such as in an exhibit to a service contract, may well exist as a means of compromise. From a carrier's perspective, many wish to allocate risks to their shippers, disclaim or limit liability, give broad continuing lien rights, and have control over the modification of what would otherwise be fixed terms under a service contract. Incorporating Carrier Terms presents certain risks for shippers, primarily on these issues of liability, indemnification, cargo loss and damage, and the fact that carriers can make unilateral changes to terms, rules, rates, and charges after satisfying their notice requirements. Shippers often make concessions and incorporate Carrier Terms, which may be warranted depending on volume needs. However, building additional terms into the service contract that incorporate Carrier Terms can help mitigate their effect by: (1) ensuring there is a strong order of precedence provision so that the service contract supersedes and controls in the event of conflict with any Carrier Terms; (2) attaching the then-current Carrier Terms as an exhibit to the service contract and specifying it will apply as-is for the term to nullify the application of any subsequent changes; and (3) calling out in the service contract that any conflicting Carrier Terms will not apply between the parties.

Benesch is well-versed in representing shippers, NVOs and carriers in all aspects of ocean transportation contracting as well as global supply chain compliance.

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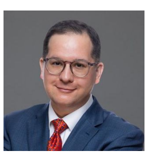

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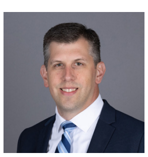

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