WHITE PAPER: SPIREON - COST SAVINGS

Fleet Costs: Where Are Successful Companies Finding Savings?

Controlling operational costs is a key priority for every fleet manager, but not every manager is successfully at reining in these costs. This begs the question - what separates the good managers from the great ones?

To answer that question, we recently hosted a masterclass budgeting webinar with Chris Henry, a Program Manager at the Truckload Carriers Association, who works with companies to lower costs and maximize savings.

Together, with Chris Henry, we conducted a deep investigation into the five major cost centers of fleets, including fuel-spend, maintenance, and driver retention, to discover methods fleet managers can use to save money and make their operation more profitable. In this white paper, we'll provide an overview of the five major fleet expense areas, share financial strategies that you can use to slash your costs, and provide real-life examples of how Sharp Transportation, a FleetLocate customer, has used these methods to realize savings.

SAVINGS AREA #1: FUEL OPTIMIZATION

Savings HIGH Potential

Fuel represents the number one business expense for fleets and 53% of fleet owners admit they have challenges controlling it, according to a recent industry survey. These findings are not surprising in an industry where carrier profit margins are razor thin and the threat of skyrocketing fuel prices is ever-present. While fuel spend is often one of the biggest and most unpredictable costs for fleets, there are still ways to minimize the damage and even find savings.

Idle Time

The single biggest culprit behind higher fuel costs is idling. When a truck idles, it can burn one gallon of fuel per hour without traveling anywhere. Beyond wasting fuel, idling can also reduce the lifecycle of your truck. An hour of idling by a heavy-duty vehicle equals approximately 80 miles of wear-and-tear on the engine. If you want to minimize fuel spend, lower your maintenance costs, reduce harmful exhaust emissions, and boost your vehicle's resale value, idle reduction should be your top priority. With a strong idle reduction policy in place combined with driver training and fuel-efficiency technologies, you can reduce this wasteful profit-draining behavior.

You can't manage what you can't measure. To create a successful idle reduction campaign, the first thing you need to do is establish a baseline and track where your fleet's current idle numbers are. This will allow you to determine whether or not each change you implement is working to save you fuel.

One of the most useful tools fleets have available to track their idle hours is telematics. With telematics, solutions like FleetLocate, you can measure down to the minute how long vehicles were idling and can even track idle time across fleet vehicles or break it down further to individual drivers per day or week. 66% of FleetLocate customers report that they were able to reduce idle time by 10-25%.

Supercharge your Fuel Surcharge Program

Another area where you can capture savings is in your fuel surcharge program. A fuel surcharge helps you cover the cost of fuel incurred during the delivery by transferring some of the expenses over to customers. To do this, you adjust the cost of hauling freight by taking into account the variation in fuel prices using historical data and tack that on to the freight charges using either a per-mile or percentage basis. These rates are typically negotiated with the customer. Creating a fuel surcharge program helps protects carriers from extreme price fluctuations and adds clarity to the billing process for your customers. There is no set industry standard for calculating surcharges, but formulas typically include the following three factors:

- A base fuel price
- A base fuel mileage of your trucks
- And the source and interval of the current fuel price

Fleets can leverage technology, like fleet management software, to develop a more accurate fuel surcharge rate. Fleet management software tracks fuel usage and miles traveled for every shipment or route. With this data, you can calculate your exact fuel-spend, save money, and offer your customers a more competitive rate

Sharp's Fuel-Spend Reduction Strategy

To save on fuel spend, Sharp has turned to technology to track and control profit-wasting idle hours. "We have real-time telematics to track idle time" and with it, Chris says his fleet's "idle time stays really, really low." When those idle hours do unexpectedly spike up, Chris stresses that communication with the driver is more valuable than handing out consequences. "You just have to have that conversation with the driver 'what's the deal, why is your idle bumped up…from 5% to 15% this month,'" Chris says, "and usually they will tell you what's going on." While he tries to educate and train his drivers on limiting this wasteful behavior, he does have to rely on other fuel-saving technologies in the event idling occurs. "We do have an idle shutdown," Chris explains. "If they are idle for five minutes, that's where the truck shuts over to the APU which still keeps the driver comfortable, warm in the winter, cool in summer. It just turns about a tenth of the fuel that the truck does." Chris can't control human behavior, but by implementing these technologies, he's got a better grasp on idle costs.

SAVINGS AREA #2: DRIVER WAGES AND BENEFITS

Savings LOW Potential

As most carriers know, the driver shortage is here—and it's getting worse. The American Trucking Association (ATA) estimates the industry is short 50,000 drivers. That number is expected to skyrocket to 175,000 by 2025. This shrinking driver pool has put pressure on many companies to increase their pay rates, offer hefty sign-on bonuses and add benefits to their overall compensation package to recruit and retain enough drivers to meet the booming freight demand. As long as the driver shortage continues, you can expect to find very little room for savings in this area.

Per Diem Payments

However, companies have found one way to soften the blow of these expenses and even offer their drivers more money: per diem payments. Per diem is the reimbursement paid to drivers for costs they incur while on the job, such as meals and other incidental expenses.

Previously, drivers were allowed to take per diem allowances as individual deductions, which reduced their taxable income and put more refund money in their pockets. However, a recent tax law, called the Tax Cuts and Jobs Act, eliminates per diem payment deductions for drivers, but still allows carriers and owner-operators to continue deducting per diem payments on their taxes. While this may sound like bad news for drivers, Chris Henry suggests it could be a win-win for all parties. With per diem, Chris Henry says, "There is a unique opportunity for you to give your drivers a little bit more, after-tax dollars and you to save some more." The trick is for the carrier to pay the per diem as a tax-free reimbursement. If a company provides per-diem to drivers on a pre-tax basis, the driver would essentially receive "tax-free" income. By offering drivers per-diem to drivers, you can relieve some of their tax burdens and use this benefit as a recruitment and retention tactic.

Workers Comp & Health Insurance

Health care and workers compensation are essential components of an employee benefits package, and therefore an important tool to recruit new talent and keep your current drivers behind the wheel. The problem is that these are the most expensive benefits to provide. Driver benefit costs increased 18% from 2015 to 2016, according to the American Transportation Institute, and are expected to continue to rise.

So how do you reduce these costs without taking away benefits from the drivers? Chris Henry believes the solution might lie in captive health insurance programs. By moving into a captive program, he says there's an opportunity for fleets of all sizes to "save on premiums, or offer, in some cases, more benefits for the same premium." However, Henry says, companies need to have an "appetite for risk." A captive insurance program is one in which costs and risk are spread out among those who invested money in the program. The benefit is that participants can pay premiums based on risk, rather than the market price, but because you share the risk of all participants this means you can either win as a team or lose as a team. For instance, if the program is made up of a collection of fleets with good safety records, then premiums go down and the "investors" see a return on profits. If participant members are operating in an unsafe manner or file more claims, then all the members lose money. Members of captive insurance programs can determine who is accepted into the group and can turn away high-risk carriers. Joining a captive might not be the best solution for your fleet, but for those that are tired of paying higher insurance costs, despite consistently good driver records, it's a viable way to achieve stable prices and increased control.

Sharp's Driver Pay Savings Strategy

To attract and retain drivers, Sharp increased driver base pay and per mile rates over the last two years, but they didn't stop there. Looking for smarter ways to manage driver pay, Chase Adkins engaged an outside accounting firm to assess what they could offer on per diem. "We added about 3.5 cents a mile per diem, Chase says, which brought them up about 8 cents [per mile] total." At Sharp, this resulted in benefits for all parties involved. "That gave us some savings and it also didn't really increase the tax burdens on our drivers a whole lot," Chase explains. Companies like Sharp understand that wages are a major factor in driver retention, but that doesn't mean giving drivers the pay they deserve doesn't have to send you into the red. "If you are going to keep drivers, you're going to have to pay them," and Chase says, "With the per diem, it kind of offset some of that increase costs that we were expecting with driver base wages going up."

SAVINGS AREA #3: EQUIPMENT FINANCING/ SPECS

Savings MED Potential

To lease or not to lease, that is the question – albeit, not a simple one. Funding your fleet requires extensive analysis and research, as a new acquisition impacts fleet performance, cash flow, and most importantly, your balance sheet.

When companies decide to acquire assets, they have two choices: leasing or buying. There are different reasons to finance or lease, and some companies do a mix of both—purchase some assets, acquire others on a full-service lease. There is no right or wrong answer to buy vs lease questions. The decision ultimately depends on the organization, how many trucks the needs, whether they have the resources to maintain them, and their current tax situation.

Typically, fleet managers will buy with cash or finance ownership if their primary business operation is primarily supported by trucks, like companies that sell fuel and need truck to make deliveries, or if the opportunity cost is lower than the cost of borrowing or leasing. Fleet managers and other decision makers should conduct a vehicle lifecycle replacement analysis before any decisions are made to determine the optimal amount of year each individual truck should be operated. With this information, you can make savvier acquisition decisions and discover the operating age in which vehicles costs more to maintain a truck than it does to replace it with a newer, more efficient vehicle. Fleet manager should also consult with their maintenance department as their insights can help you determine the true cost of ownership.

Fleets that lease vehicles typically are larger in size or don't have the funds to keep up with maintenance gravitate toward. Leasing offers many benefits, such as lowering the total cost of ownership, reduced maintenance fees, and the ability to run newer equipment more often. It's typically a roll of the dice trying to anticipate future interest rates, but with the recent tax reform law that has lowered the tax rate to a flat rate of 21%, the current market is favorable for leasing equipment. In addition, today's technician shortage might also influence your decision to lease as leases take this burden off of you. If your operation relies on extremely unique equipment specifications or if you intend to run longer replacement cycles, then ownership might be more beneficial. With that said, leasing offers a wider range of savings and benefits for fleets looking to reduce their operation costs.

Sharp's Financing Strategy

Sharp's strategy to financing? Divide and conquer. Chase says, "We don't put all our eggs in one basket, as far as financing goes; we kind of spread it out with different banks, both national and local." By relying very little on OEM financing, Chase says he's able to get the most competitive rate because he's shopping each time.

FleetLocate BY SPIREON

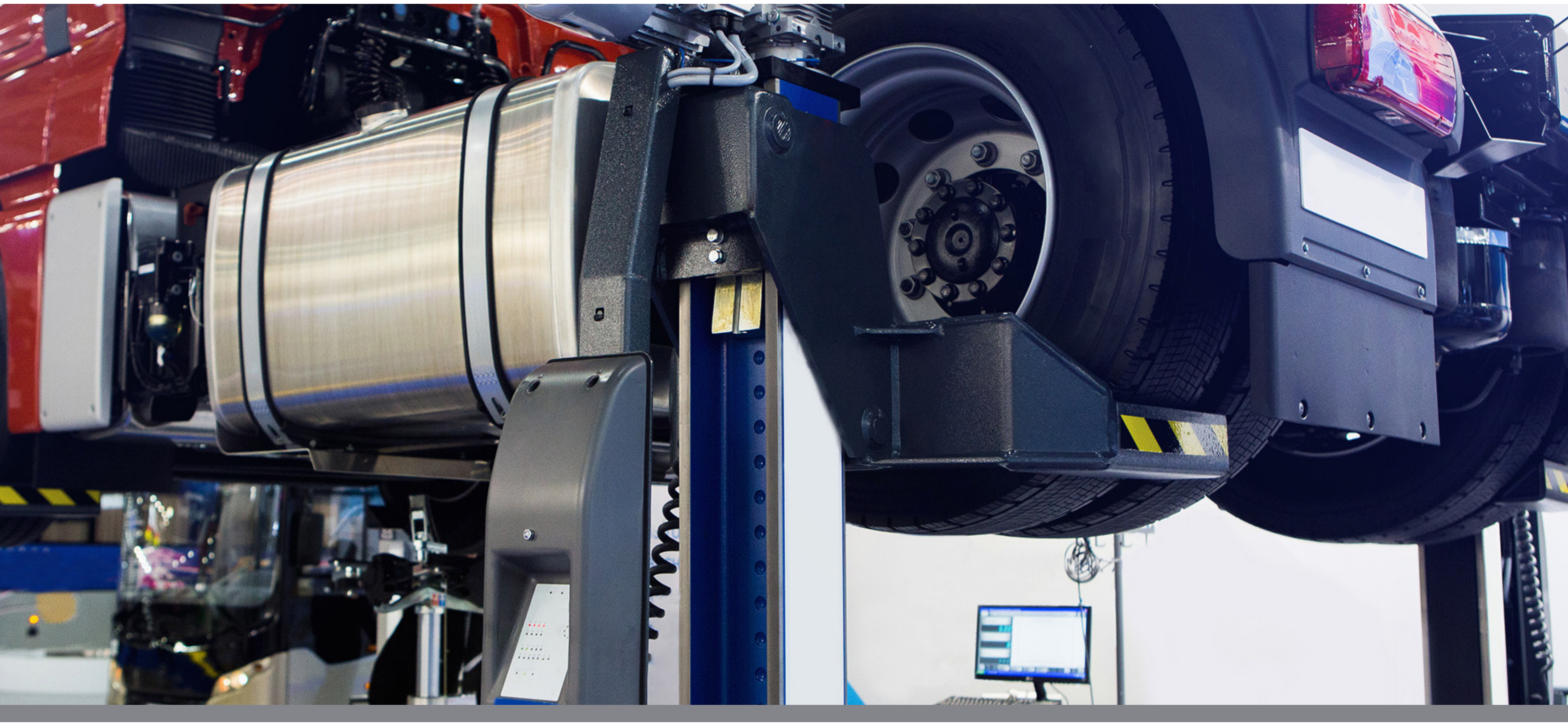
SAVINGS AREA #4: MAINTENANCE

Savings HIGH Potential

According to a recent survey we conducted, 45% of fleet owners say vehicle maintenance is one of their biggest cost concerns. Findings from the American Transportation Research Institute validate those fears, as this line item cost went up seven percent from 2015 to 2016, reaching \$0.166 per mile – the highest level recorded in the survey's history. These increased maintenance costs can be attributed to the fact that fleets are driving more to meet increases in freight demand. More miles means more wear and tear on trucks. In addition, today's mechanic shortage and technologically advanced vehicles are driving up costs, due to the specialized labor that's needed to repair and maintain these sophisticated systems.

While preventative maintenance program can help you avoid costly breakdowns and extend the lifecycle of your vehicles, these expenses can spiral out of control if not monitored properly. Companies should work together with their maintenance team to track all the costs associated with maintenance and determine where improvements can be made.

You can't cut your maintenance costs if you're not tracking them in the first place. Carriers should create a spreadsheet that tracks each breakdown, which components failed, at what mileage, and the total direct and indirect costs of each breakdown (i.e. motel fees for sidelined drivers, renting a replacement tractor, towing fees, total labor costs, etc.). Armed with this data, you can determine if it's more economical to repair or replace malfunctioning items, whether you should handle the maintenance internally or outsource it to a vendor, and how effective, or ineffective, your technicians are.



Lowering Replacement Cycles

If you want to save money on maintenance costs, consider lowering your vehicle replacement cycles. In the same way people develop more health problems as they age, vehicles need more maintenance and repairs the longer they're in operation. An industry report by Fleet Advantage concluded Maintenance costs for vehicles aged 4-6 are 2.75 times higher than they are in years 1-3. Fleet owners have three solutions in this scenario – hire more technicians, acquire more spare trucks, or replace assets that are past their prime. Letting go of aging assets and using shorter truck replacement cycles yields the greatest savings. According to that same study, fleets who adopt a three-year vehicle lifecycle and replace equipment in year four can see savings of $42,830 in maintenance and repair costs alone, compared to a truck with a seven-year replacement cycle.

Fleet owners should consult with their maintenance team and use data-driven analytics to determine the replacement cycle that's best for their fleet. Data from telematics and maintenance tracking software can help fleets accurately pinpoint the costs it takes to maintain vehicles and if these costs are economically justifiable. Armed with this information, businesses can make smarter decisions that help them reduce breakdowns, maintenance costs, and technician labor fees.

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Warranty Capture

Nearly all new parts, systems, and vehicles that you purchase come with a warranty that's built into the price. Since you've already paid for that warranty protection, it makes fiscal sense that you should get every return possible. Studies show that the return on warranty can be as high as 20:1, making it one of the more profitable areas in fleet operations. Unfortunately, many fleets never realize these savings and pay for repairs or parts that are actually covered under their warranty. To make sure your capturing every dollar and avoiding unnecessary repair costs, you need to develop a process to manage and track warranty eligible items in your inventory.

Start by having a dedicated warranty manager that oversees warranties across your entire fleet. Each OEM has its own policies that can vary in this and that way. Before submitting a claim, managers should fully understand the terms and conditions of warranty policies for each different piece of equipment. To prevent warranties getting rejected due to improper repairs, make sure your mechanics are trained on the proper warranty process for each piece of equipment.

Sharp's Maintenance & Repair Savings Strategy

Chase Adkins says the number one key to lowering his maintenance costs was lowering replacement cycles. "Some of the stuff that we were outsourcing before, like major overhauls, engine rebuilds, the stuff that -- it takes a lot more time when we kept trucks longer," but Chris says now that they've shortened their replacement cycle, they "dropped external spend down a little bit."

SAVINGS AREA #5: VEHICLE INSURANCE PREMIUMS

Savings HIGH Potential

Trucking demand is booming, and although this is good for business, it comes with inherent risks. More freight demand means more time spent on the road, and thus increases the likelihood that you'll get into an accident. This increased road time, combined with a distracted driving epidemic and a litigation-prone society, has created the perfect storm for higher insurance premiums. According to the Motus Driver Safety risk report, companies lost nearly $57 billion in accident costs in 2017. These losses are resulting in higher premiums for fleets of all types and sizes, from owner-operators to major corporations. Even though the trucking insurance market continues to harden, you can still save money through effective risk management policies and by exploring captive insurance programs.

Managing Risks & Driver Safety

Ensuring your fleet is running safely is not only the right thing to do; it also directly affects your bottom line. Safer carriers are more profitable carries. Lower CSA scores and lower claims on file result in lower premiums. With an effective safety management program in place, you can see returns that reach far beyond lower premiums, such as:

- Reduce medical expenses and workers compensation
- Reduced downtime and vehicle repair costs
- Increased driver and vehicle productivity
- Improved driver morale

To manage your risks and reduce your exposure to premium hikes, companies need to develop an iron-clad safety policy that every member of fleet operations adheres to. This can include driver training, coaching, and quarterly safety reviews to find areas of improvement. As part of your risk management policy, Chris Henry recommends tracking accident repair expense to find a "golden nugget" of savings. "Based on my experience," Henry says, "there is a direct correlation, I don't know if it's anecdotal or just simply valid that a lot of the top performing companies are tracking things like accident repair expense at the geo level instead of it just flowing through to maintenance and following where it may."

Fleets should also consider adopting safety technologies, such as telematics, to manage their risk profile and bring down insurance costs. With telematics you can identify risky on-road behaviors, like speeding and hard braking, to correct unsafe driving practices before they result in a violation or accident.

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Sharp's Insurance Savings Strategy

To reduce their insurance costs, Sharp joined a captive insurance program, and while there's more risk involved Chris believes it's well worth it. "You treat claims differently when you have a claim when you are in a Captive because you have more skin in the game than you do when you have traditional insurance," but overall Chris says, "We have had positive results."