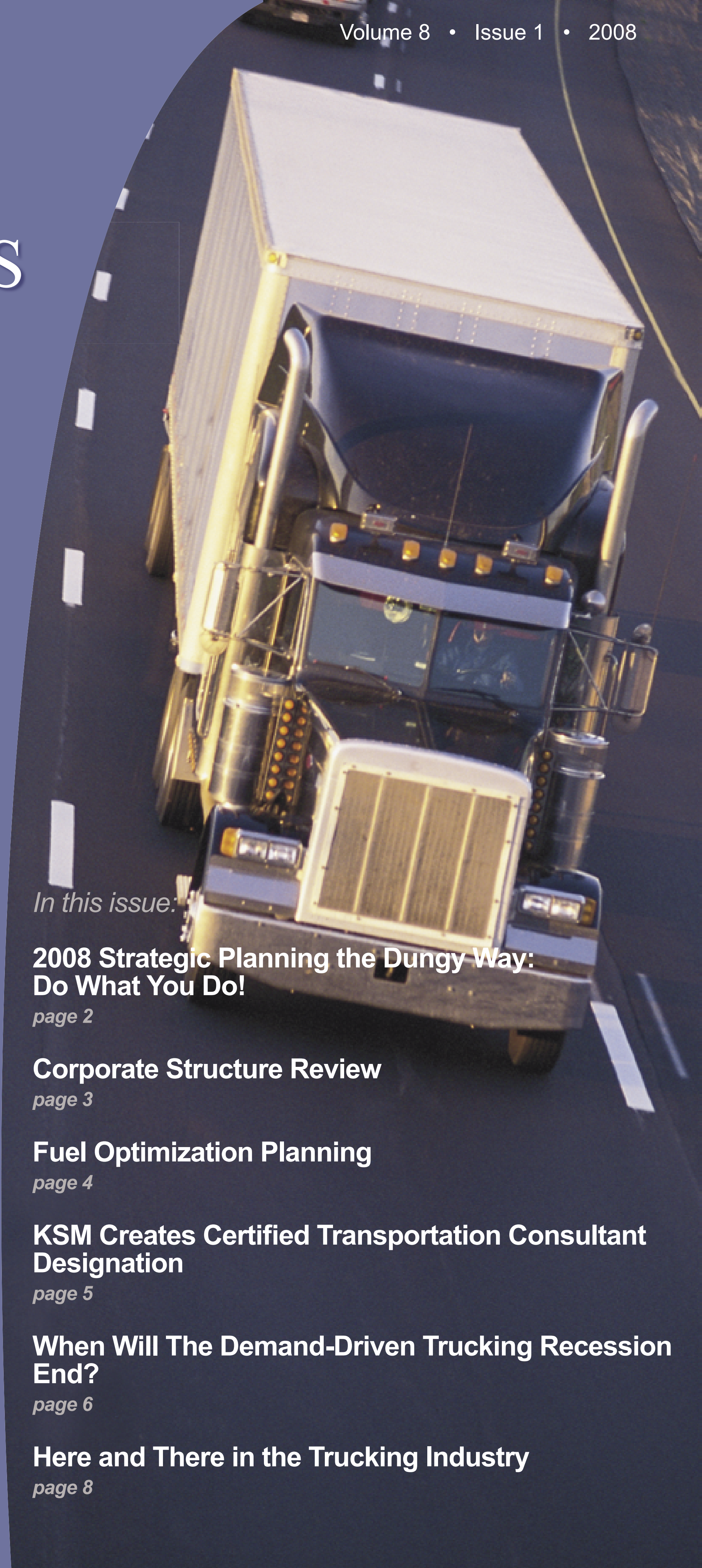
Volume 8 • Issue 1 • 2008

KATZ, SAPPER & MILLER

TRUCK TIMES

The Financial Side of the Trucking Industry



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2008 Strategic Planning the Dungy Way: Do What You Do!

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In his best selling book, "Quiet Strength," Tony Dungy, coach of the Indianapolis Colts, outlined the list of goals that he has used for every one of his training camps:

- Top 5 in the NFL in giveaway/takeaway ratio
- Top 5 in the NFL in fewest penalties
- Top 5 in overall special teams
- Make big plays
- Don't give up big plays

He also communicates with the team what is expected of them:

- Be a pro.
- Act like a champion.
- Respond to adversity; don't react.
- Be on time. Being late means either it's not important to you or you cannot be relied upon.
- Execute. Do what you're supposed to do when you're supposed to do it. Not almost. All the way. Not most of the time. All of the time.
- Take ownership.
- Whatever it takes.
- No excuses, no explanations.

> *"Be patient, keep doing the ordinary things better than anyone else. Be uncommon. Do what we do."*
>
> *- Tony Dungy*

After the Colts lost to the Jets 41 to 0 in the 2002 playoffs, Dungy did not waiver from these goals and values. He told his team "Be patient, keep doing the ordinary things better than anyone else. Be uncommon. Do what we do." Sticking to these values and goals has resulted in the Colts winning the 2007 Super Bowl and Dungy's team being in the playoffs for nine consecutive years. An achievement only matched by Hall of Famer, Tom Landry of the Dallas Cowboys.

What are the company's goals and strategic plan for 2008 and beyond that will help achieve a consistent high level of performance similar to Dungy's team? Many trucking companies will not invest the time to formalize a strategic plan because they believe that setting strategy is complicated or can only be done by consultants. As noted from Tony Dungy's strategic plan, it does not have to be complicated. Keep it simple; just "do what you do."

Jim Collins, author of "*Good to Great*" and "*Built to Last,*" believes strategy is simply the basic methodology a company intends to apply to attain its current mission. He outlines four key principles in setting company strategy:

- It must descend directly from the company's vision. Strategy cannot be set if there isn't a clear mission, purpose, core values and beliefs. Vision first, then strategy!

- The strategy must leverage off the strengths and unique capabilities of the company. This involves a clear assessment of the strengths and weaknesses of the company. Ask the management team, "What are we better at than anyone else that gives us a competitive advantage?"

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Corporate Structure Review

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Given the litigious nature of society, it is easy to imagine a court or jury awarding huge judgments to plaintiffs involved in a catastrophic accident with a trucking company. There have been several recent examples where damages have been awarded that well exceed insurance coverage of the trucking company. At times, the awards even exceed the actual value of the trucking company. In addition to regular insurance, many trucking companies have examined their own corporate structure as a way of further protecting their valuable assets from the high risk of running a trucking operation.

"...if a corporate structure involves multiple companies, they should do their best to handle the business between each entity as if it were being conducted with a third party."

Over the past several years, the trend of trucking companies has been to form separate companies for handling certain components of the overall freight services supply chain. The separation might include an equipment leasing entity, the trucking company, a logistics company, a brokerage operation and separate real estate rental companies to own the terminals and offices. While it is generally agreed upon that separate companies is very beneficial in the protection of assets compared to the alternative of one single company owning all assets, the extent to which the protection shields liability from one entity to another requires advice from legal counsel. Regardless of the potential benefits, it is highly advisable to manage and account for separate entities at arm's length from one another. In other words, if a corporate structure involves multiple companies, they should do their best to handle the business between each entity as if it were being conducted with a third party.

The pricing, contracting and payment of services among various entities are important in a series of steps that should be routinely reviewed by each company. First, formal agreements for transactions among related companies should be in place. Examples of these include lease agreements, brokerage agreements, administrative service agreements and inter-company loan agreements. As the trucking company grows and evolves, these agreements must be modified and updated to adapt to changes in conditions.

The agreement pricing should have economic substance; in other words, the charges should follow the fair value concept at prices that could be regularly negotiated in the marketplace. Of course, there is latitude as fair value is often times a subjective concept, but a good faith effort at pricing should always be maintained. The value of inter-company charges is also an area of focus for IRS audits.

Although many trucking companies do a good job of creating agreements among companies, several fall short on the maintenance of these documents. For example, many times, audits or reviews of financial information have found that companies do not regularly invoice for inter-company charges and/or pay these invoices on a separate and timely basis. Often, companies transfer cash only as needed for business cash flow purposes rather than at an arm's length fashion of regular payment (much the same as a company would

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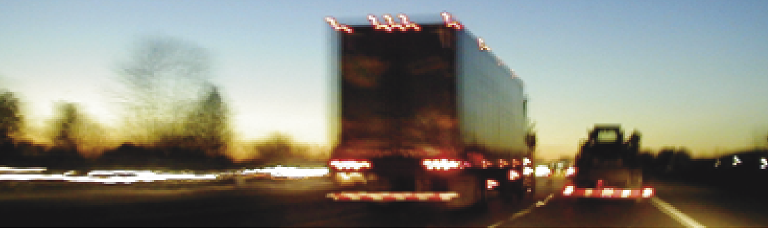

Fuel Optimization Planning

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Almost all transportation companies use fuel network-agreements to obtain the best fuel pricing. Company polices and procedures are normally in place to maximize compliance among drivers to fuel within the network. However, there are common misconceptions, such as; more money can be saved by concerting the most gallons in the fewest number of locations, or that the network arrangement is providing the lowest cost available.

"Use of a fuel optimization plan can result in a 4 to 7 cent per gallon savings and virtually eliminate out-of-route miles related to fueling."

Often retail fuel prices can vary greatly among truck stops along a given route within the network. Network negotiated prices are based on a percentage or an amount discounted from the retail pricing resulting in trucking companies' fuel cost being greater than if properly managed with planned fueling at the lowest cost points along a route. It is not uncommon for fuel cost to vary as much as 37 cents a gallon along a given route.

Fuel optimization software utilizes current technology by adding fuel price and routing data to deliver drivers with optimized fuel purchases and routing plans at the time of dispatch. The optimal fuel purchase plan is constructed based on current fuel prices along the dispatched route. By measuring true fuel cost, taking into account network discounts, state fuel tax and tolls, the plan predetermines and schedules refueling stops.

The fuel optimization software provides compliance reports by truck, an audit of fuel charges and "what if" analysis for fuel network design and price discount structures. Use of a fuel optimization plan can result in a 4 to 7 cent per gallon savings and virtually eliminate out-of-route miles related to fueling.

Factors considered in a fuel optimization plan include tractor location, fuel capacity, fuel consumption, route, truck stop required amenities, tank fill policy, minimum fuel levels and tax implications in developing the best plan at dispatch. •

Example of Fuel Optimization Plan

Assumptions:
Fleet of 100 tractors
Each averages 100,000 miles per year
Average 6 miles per gallon
Estimated 5 cents per gallon saving with plan

Tractor Fleet	100
Annual Miles Driven per unit	100,000
Total Miles	10,000,000
Average MPG	6
Gallons of Fuel Used	1,666,667
Savings with Fuel Optimization Plan	$0.05
Estimated Annual Savings	$83,333

KSM Creates Certified Transportation Consultant Designation

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In November, more than 40 KSM professionals completed the first step in becoming a KSM Certified Transportation Consultant (KSM CTC). The KSM Transportation Group created the Certified Transportation Consultant designation as a commitment to educate and train new trucking service team professionals on the history, current economic trends, tax, audit and operational issues facing trucking companies.

To receive the KSM Certified Transportation Consultant ranking, KSM professionals must complete the following requirements:

- Complete "Trucking Basics 101"
- Attend the annual KSM trucking industry update
- Be a team member of at least 5 trucking engagements
- Attend a KSM trucking roundtable or industry event each year
- Work a day in the operations of a trucking company
- Write an article for KSM's *Truck Times* or other transportation publication/or give a presentation
- Read one business book or a book on the trucking industry and present to the KSM Transportation Group

Trucking Basics 101 is divided into four general sections. The course is an overview of the industry which includes a brief review of the history of trucking, the current economic environment, a review of the trade groups supporting the industry and acronyms and terms. Tax issues and structures particular to trucking and audit areas of concern and recent developments are also presented. Lastly, operational issues and key performance indicators are highlighted, including managing idle time, out-of-route miles, fuel cost, maintenance issues and managing accounts receivable. •

Do What You Do *(continued from page 2)*

- The strategy must be realistic. It must take into account internal constraints and external factors such as competitors and customers and the economic and regulatory environment.

- Strategy should be set with the participation of those who are going to be on the line to make it happen. Once the strategy is set, specific accountable action steps will be established (who is to do what, by when and how).

Dungy's coaching philosophy was influenced by one of the best, Chuck Noll of the Pittsburgh Steelers, who said "champions are champions not because they do anything extraordinary, but because they do the ordinary things better than anyone else." •

When Will the Demand-Driven Trucking Recession End?

The following is an edited transcription of a presentation John Larkin, managing director of Stifel Nicolaus Transportation Research, delivered November 15, 2007, before an audience of industry professionals at the Ontario Trucking Association Conference.

Conflicting Economic Data Abounds

There's a lot of conflicting economic data out there. GDP growth was 3.9% in the third quarter and 160,000 jobs were created last month. It does not feel like a recession when you look at those numbers, yet banks are tightening credit across the board. We are seeing defaults increase on adjustable-rate mortgages. We are seeing the housing industry in shambles and we are seeing truck tonnage declines in 17 out of the last 21 months. So it depends on your perspective; but there are lots of warning signs on the horizon. Hopefully, Fed Chairman Ben Bernanke will help us through this with further rate cuts.

Freight volumes have shown few signs of recovering

Freight volume has shown no real signs of recovery. The first robust date that we have seen on a year-over-year basis was rail data during the month of November. 3% ton-mile growth, year-over-year, during the week of November 17 and 6% ton-mile growth the previous week are pretty interesting numbers. Two weeks do not make a long-run trend, but it is interesting to consider.

Longer-term outlook suggests tight supply and demand

The longer-term outlook suggests to us that supply and demand will be tight. It's hard for us to envision tight supply and demand in the immediate term, but the driver situation presents a long-term problem. Highway congestion is also a long-term problem. In addition, the lack of a national transportation strategic plan is also a big problem, in our view.

"The longer-term outlook suggests to us that supply and demand will be tight. In addition, the lack of a national transportation strategic plan is also a big problem."

Truckers are shouldering most of the current economic pain

Truckers are shouldering most of the current economic pain in the freight transportation industry, in our view. The railroads are somewhat sheltered by virtue of the fact that they haul imports and exports, which are pretty strong right now. The rails should continue to do well hauling energy; people are going to continue to heat their homes, whether GDP is growing at 1% or 3%. The agriculture boom, mostly fueled by the ethanol boom, really has been a shot in the arm for the railroads.

E-commerce is certainly helping UPS and FedEx, and the globalization of the world economy is certainly helping them as well. So the truckers are taking the brunt of the economic pain, and within the trucking industry, the truckload carriers appear to us to be taking it more directly than the LTL carriers. •

Reprinted with permission of John Larkin, managing director of Stifel Nicolaus Transportation Research.

Corporate Structure Review *(continued from page 3)*

do for its third-party vendors). Rate structures can also be inconsistent with a company's cash flow requirements and business expenses of the entities. The result may be having a cash shortfall where not desired or surplus where not optimal.

The trend of separate structure of entities in trucking operations will continue, however, it is important to take a step back and review the big picture to see if it still makes sense to have separate companies. The obvious issue to consider is the overall cost versus benefit of having the added burden of governance of numerous entities. In some cases, the complexity may simply be too burdensome and cause confusion and poor execution. It may make more sense to focus efforts on a stronger driver safety program rather than a burdensome restructuring as a means to reduce risk. Of course, there is no better protection than having sufficient insurance coverage.

"If a trucking company has multiple entities, it is recommended that the company regularly reevaluate the operations. Trucking owners must analyze whether or not their plan and structure are accomplishing their goals and objectives."

Another area of consideration is the preservation of wealth on the balance sheet of the stronger performing companies. Cash reserves and excess assets would be best left to accumulate outside of the actual trucking company. Many times in corporate structures there is a parent holding company that owns the operating entities. Perhaps the subsidiary should declare a dividend and disburse excess earnings up to the parent company. Should the operating subsidiary ever have a need to draw on these excess funds, the parent could execute a loan to the subsidiary rather than make a permanent contribution of capital.

The owners and financial managers should also reconsider the capital structure of the various entities and analyze whether the entity is properly capitalized to finance and support the operating requirements of the entity. For example, have inter-company loans been made from one entity to another wherein the repayment of such loans is highly unlikely over the next five years? Perhaps in this case the better solution might be to make a permanent infusion of capital to properly fund the business; particularly if the entity is thinly capitalized. Or perhaps the operating subsidiary simply has too much retained capital and it would be best to permanently distribute the capital to the parent company or owner.

In summary, if a trucking company has multiple entities, it is recommended that the company regularly reevaluate the operations. Trucking owners must analyze whether or not their plan and structure are accomplishing their goals and objectives. Also, they should determine if their goal is to seek legal protection of assets or just to measure performance. Regardless, it is extremely important for owners to do more than just implement a plan; they must regularly execute it and, most importantly, be willing to reevaluate its effectiveness and make required changes to agreements or capital structures. •

Here and There in the Trucking Industry

Tim Almack and Marty Wright attended the Indiana Motor Truck Association's Annual Convention in Bonita Springs, FL.

Tim Almack attended the Kentucky Motor Truck Association Board Meeting in Owensboro, KY.

Tim Almack spoke on Accounting, Tax and Key Performance Indicators at the Indiana Motor Truck Association's Future Leaders Conference.

Tim Almack, Mark Flinchum, Marty Wright and Jason Miller presented "Trucking Basics 101" to KSM staff.

Andy Belser attended the National Accounting and Finance Council Conference in Denver, CO.

Mark Flinchum and Chris Cox attended the Indiana Household Movers and Warehousemen Annual Convention.

Bruce Jones attended the Tennessee Trucking Association Convention in Destin, FL.

Marty Wright participated in the Indiana Motor Truck Association's Future Leaders Conference.

KSM's Committment to the Trucking Industry:

- American Trucking Association
- Illinois Trucking Association
- Indiana Motor Truck Association
- Kentucky Motor Truck Association
- National Tank Truck
- Ohio Trucking Association
- Truckload Carriers Association
- Tennessee Trucking Association

For more information about Katz, Sapper & Miller, please visit www.ksmcpa.com.

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