

# SURF & TURF

LEGAL NEWS IN TRANSPORTATION & LOGISTICS

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## 10+2: CUSTOMS AND BORDER PROTECTION'S SIMPLE MATH CREATES COMPLEX PROBLEMS

By Steve Block

Earlier this year, U.S. Customs and Border Protection ("Customs") issued a notice of proposed rulemaking, currently the subject of comments, regarding possible new requirements for reporting particulars about inbound cargo. The concept involves lining up ten new hoops importers must jump through to get their cargo cleared through Customs' Automated Targeting System ("ATS"), and two new ones on the already complex obstacle course carriers operate on. The program is known as "10+2," a title that might imply a simple, trouble-free system. However, industry's reaction suggests it would be anything but that.

ATS has already gotten its share of bad press. The centralized and computerized system originally was enacted to process inbound international freight, taking advantage of technology that would allow coordinated analysis of threat, administration of security, and implementation of law enforcement if/when needed.

But when Customs decided a couple years ago to apply this technology to travelers crossing the Canadian and Mexican borders, civil rights groups immediately cried foul. It's one thing to be "targeting" cargo coming from overseas; it's quite another to do so against American tourists coming home from a Cinco de Mayo celebration. Despite some concessions and promises from the feds regarding privacy and usage of acquired intelligence, the dickering continues.

10+2, if adopted, would add new terms to the "24-Hour Rule" which was implanted not long after 9/11. That rule, too, was the subject of some importer heartburn, as it mandated that shippers and importers advise Customs of every cargo's exact destination a full day before stowage on a vessel (a detail larger importers don't always know that early). The 24-Hour Rule also forces international players to rely on Customs' promise to keep business secrets

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confidential, which some folks have a tough time embracing.

The Security and Accountability for Every Port Act of 2006 (the "SAFE Port Act") went into effect on October 13, 2006, and required Customs to gather data beyond what the 24-Hour Rule currently gets from shippers and carriers heading stateside. If adopted, the new reg would require importers to state the following ten items a full day before their freight is even placed on a U.S.-bound vessel: (1) manufacturer's/supplier's name and address; (2) seller's name and address; (3) buyer's name and address; (4) "ship-to" name and address; (5) container stuffing location; (6) consolidator's/stuffer's name and address; (7) the importer of record; (8) consignee number(s); (9) country of origin; and (10) the commodity's HTSUS (Harmonized Tariff Schedule number). Considerable detail about some of these items also is required in the electronic reporting.

Carriers would have to present within 48 hours after departure (1) a vessel stow plan for vessels headed to the States; and (2) container status messages, which would ensure the feds keep abreast of the chain of each container's possession en route to the U.S. Like importers, carriers would have to provide detail about their data submissions.

## 10+2 ... (Continued)

Customs makes a good argument that the additional information would facilitate the agency's efforts to combat terrorism, and is necessary for compliance with the SAFE Port Act. Moreover, Customs is quick to point out that C-TPAT membership would still produce that friendly nod of approval at the border, and would ensure favorable treatment by Homeland Security on complications.

While no one minimizes the importance of fighting terrorism, the shipping community has issued less than favorable reviews of the proposed new regs. The European Shippers' Council ("ESC") thinks the burdens created by 10+2 would be too much hassle for shippers on the Continent - especially those with high volumes - to live by. In addition to trade secrecy concerns, ESC points out that the 10+2 program would go far beyond what earlier was recommended by the World Customs Organization.

Others complain that no matter how well-intended the program might be, some of the extensive data it would require simply isn't available that early in the process. Moreover, the more info Customs requires under early-deadline conditions, the more techno-savvy all concerned have to be. The costs of keeping more computer geeks on staff (along with additional hard and software) don't make the program any more inviting.

Like so many other counterterrorism issues of the modern era, 10+2 calls for a balancing act between valid government and social concerns on the one hand, and the capacities, realities and interests of the trading community on the other. The proposed program demonstrates a need for better technology and government regulation of industry activities in ways that would ease the burden on those who want to join in the effort to prevent another terrorist tragedy.

Ref: Notice of proposed rulemaking, available at <http://a257.g.akamaitech.net/7/257/2422/01jan20081800/edocket.access.gpo.gov/2008/E7-25306.htm>; and *The Security and Accountability for Every Port Act of 2006* (P.L. 109-347).

## OCEAN TRANSPORTATION INTERMEDIARIES MAY NOT OPERATE THROUGH "AGENTS": THE U.S. FEDERAL MARITIME COMMISSION OUTLAWS UNLICENSED OTI DEPUTIES.

By Steve Block

With the proliferation of non-vessel operating common carriers (NVOCCs) and ocean freight forwarders catering to expanding international trade, it's only natural that some of these middlemen of ocean shipping have become creative in enlarging their operations. Grouped together for regulatory purposes as "Ocean Transportation Intermediaries" (OTIs), many NVOCCs and forwarders have followed the path of other service providers with multi-geographical presences, and opened branch offices in areas where business is, or might become, robust.

The OTI industry is governed by federal statute and regs promulgated and enforced by the U.S. Federal Maritime Commission (FMC). FMC requires OTIs to obtain licenses and post bonds available to aggrieved shippers as a payment source for unpaid claims. The licensing process requires applicants to have on staff a "qualified individual" (or "QI") who is familiar with ocean shipping regulation.

But with the trend toward expansion, a question has arisen as to whether each of an OTI's branch offices, particularly regarding unincorporated satellites managed directly by the mother ship, must hold its own license and post its own bond. OTI Team Ocean Services, Inc. took the question to FMC's general counsel by way of an informal inquiry process FMC offers the shipping public that is not binding on the FMC itself.

In other words, FMC's law office can tell you a proposed action would be kosher, but the commissioners themselves can disagree and still slap an inadvertent offender's hand if it relies on their lawyer's advice. When asked whether branch offices whose employees are "agents" that undertake virtually all OTI services in the name of license-holding Team Ocean need their

## OCEAN . . . (Continued)

own separate FMC blessings, FMC's attorney apparently opined that this business plan wouldn't require separate licensing. To be sure, and in coordination with other elements of the OTI industry, Team Ocean petitioned the FMC itself for a final ruling that would be applicable to the entire OTI world.

The National Customs Brokers and Forwarders Association of America (NCBFAA) chimed in, as did two other private concerns. Team Ocean, NCBFAA and another OTI pointed to the extreme difficulty - if not absurdity - of requiring agents of OTIs to be licensed and bonded, when so many service providers undertake OTI services at licensed entities' behest for any given shipment. For example, forwarders regularly engage truckers, packers, consolidators, warehousemen, and numerous others to perform essential services that properly would be classified as regulated OTI activities. If they aren't licensed and regulated - and they aren't - then why should a more closely affiliated agent of an OTI be subject to FMC oversight? Moreover, general principles of agency law suggest that separate licensing and regulation aren't warranted under these circumstances.

In issuing its order, FMC explained how mindful it was of the evolving OTI industry, and the modifications to regs it has taken in recent years to accommodate ocean shipping middlemen. Most significantly, FMC retooled its regs and enforcement procedures in 2004 to allow NVOCCS to enter into service arrangements with carriers, putting them roughly on equal footing with shippers who contract directly with steamship lines.

But in response to the current petition, FMC concluded it was bound by Congress to disallow separately situated "agents" of OTIs to operate without their own licensing and bonding. The most current version of the Shipping Act, along with Congress' stated concerns about security, preclude FMC from letting entities without an onsite QI from operating under a remotely located OTI's authority. Because the statute is "remedial" in nature (i.e., intended to provide remedies to members of the public harmed by OTI error), FMC must interpret it broadly.

Congress could and would have carved an exception if it had so intended.

If Team Ocean's petition were granted, FMC envisioned an explosion of "agents" operating nationwide under someone else's name and credentials, rendering scrutiny and enforcement impossible. The bonding requirements would become virtually meaningless, as a single bond might apply to perhaps hundreds of agents, such that effective coverage would become diluted. FMC's work with law enforcement would be weakened, as it would have less data about and control over players in international transportation.

FMC's treatment of Team Ocean's comparison of service vendors to its closely held agents is less compelling. The opinion declares there is no "bright line" as to what constitutes an unregulated OTI vendor or service provider, and an agent that must be bonded, licensed and staffed by a QI. Presumably, FMC's enforcement division will know a violation when it sees one, perhaps when the unlicensed entity actually holds itself out to the public as an OTI or deals directly with shippers and carriers à la an intermediary.

Ultimately, the circumstances surrounding Team Ocean's petition are a reflection of the successful business evolution created by ocean shipping deregulation in 1998. Unfortunately, security concerns have increased since that time, and Congress is slow to move in re-legislating shipping law. The result may be the best we could hope for.

Ref: *FMC Order*, available on the FMC's website at

[http://www.fmc.gov/UserFiles/pages/File/Commission\\_Order\\_Docket\\_No.\\_06-08.pdf](http://www.fmc.gov/UserFiles/pages/File/Commission_Order_Docket_No._06-08.pdf)



## HOT RECENT CASES IN MOTOR CARRIER LAW

By Steve Block

Transportation brokers aren't liable under Carmack, but that's not enough to defeat an amended complaint on its face.

*Electroplated Metal Solutions, Inc. v. American Services, Inc., et al*, 2008 WL 345617 (N.D. Ill. 2008)

Shipper Electroplated Metal Solutions (EMS) engaged Two Brothers Trucking to arrange transport of industrial machinery from California to Illinois. Two Brothers, primarily a carrier but also a transportation broker, placed the freight with a couple carriers. EMS' freight arrived damaged, and the shipper sued all concerned in the U.S. District Court for the Northern District of Illinois.

EMS' complaint alleged Carmack liability, a theory that fails against brokers. Carmack only holds the feet of freight forwarders and carrier to the fire of cargo liability. Thus, Two Brothers successfully moved to dismiss the complaint.

Of course, the dismissal prompted EMS to move to amend its complaint to state proper causes of action, relief federal courts grant liberally. Two Brothers opposed that motion, again pointing to Carmack's lack of any basis to hold brokers liable for cargo damage. Moreover, asserted Two Brothers, any state law claims EMS had against the broker are preempted by, well, Carmack.

The court rejected that argument. Just because Carmack doesn't concern itself with broker liability, doesn't mean there can't ever be any. In fact, the absence of attention to brokers in Carmack means Congress wanted state law to govern their liability, which is exactly what courts across the land have been ruling for years. Whether or not Two Brothers did its job right is a question of fact not properly addressed on a motion to amend a complaint. Two Brothers is back in court.

Balancing the equities: a shipper and intermediary avoid double payment of freight charges.

*Marx Transport, Inc. v. Air Express International Corp., et al*, 2008 WL 509776 (Ill.App. 1 Dist. 2008)

Here's a twist on the old carrier-seeks-payment-from-shipper-after-broker-collects-and-defaults scenario. Two middlemen - North American Expediting and Danzas - and trucker Marx Transport carrier had been in the practice of billing and collecting only from the former. When North American went belly up (rendering Marx' default judgment against it useless), the carrier turned to Danzas and shipper Corning with opened palms. The whole mess went to an Illinois court that promptly threw out Marx's claims.

The defendants first urged they had no agreement with Marx, as North American hired the trucker. Marx had issued what purported to be bills of lading. The trial court found the documents too ambiguous to be enforceable bills of lading, and dismissed Marx' claim partially on that basis. Marx sent the matter up to the Illinois Court of Appeals.

The higher court disagreed. The bills of lading contained all the basics required by law. However, an effective bill of lading doesn't necessarily show who has to pay. "Put simply, a shipper will be liable to a contract carrier if it agreed to pay the carrier." Moreover, "[t]he parties to a shipping agreement are free to contract when and who will pay the freight charges."

So what's a court to do? Somewhere, an innocent player will get screwed, either by having to pay twice or not collecting charges for services provided. Recognizing that decisions have gone in different directions on this issue - often for the same reasons - this court looked at the parties' history and interaction with each other. Affirming the trial court's conclusion (and dismissing Marx' claims), the court noted that Marx didn't actually contract with either the shipper or Danzas; didn't document who would paid freight charges; never submitted previous invoices (for similar shipments) to either remaining defendant; and apparently expected to be paid only by North American.

## Hot Recent Cases (Continued)

But going the other way, a shipper and broker are jointly and severally liable for unpaid freight charges in a complex maze of contracts and bills of lading.

*Oak Harbor Freight Lines, Inc. v. Sears Roebuck & Co.*, et al, 513 F.3d 949 (9<sup>th</sup> Cir. 2008)

This Ninth Circuit decision apparently caps off years of litigation between Carrier Oak Harbor Freight Lines, broker National Logistics Corporation (“NLC”), and consignee Sears Roebuck (that received regular deliveries from its suppliers). The long-term, volume intensive arrangement was based on a contract between Oak Harbor and NLC, outbound bills of lading issued by Sears, and return shipment bills of lading issued by Oak Harbor. Sears tendered freight charge payments to NLC, which passed them along (minus its fees) to the carrier. When Sears fired NLC, the arrangement unraveled.

Oak Harbor wasn’t paid some 426 grand in freight charges, and sued NLC and Sears in the Western District of Washington. The trial court found NLC and Sears jointly and severally liable for the unpaid freight, and appeal to the Ninth Circuit followed.

The Court of Appeals, affirming the district court’s summary judgment order, found significant Sears’ concession that it drafted its bill of lading to conform with industry standards, part of which contemplates shippers being ultimately liable for unpaid freight charges. Moreover, Sears could have protected itself by including in its bill of lading a “nonrecourse clause.” NLC’s contract with Oak Harbor provided that NLC would be liable for unpaid freight charges, but didn’t say Sears *wouldn’t* be liable. A contract does not render the bills of lading unenforceable despite precedents that would so provide if there were irreconcilable differences between the two. Lastly, equitable estoppel didn’t save innocent consignee Sears from double liability. Again, it knew or should’ve known what it was doing, and had means to protect itself.

A shipper’s Carmack claim is tossed out on summary judgment, or why cargo claimants need lawyers.

*Fraser-Nash v. Atlas Van Lines, Inc.*, 2008 WL 346381 (S.D. Tex. 2008)

Household goods shipper Fraser-Nash engaged carrier Atlas Van Lines to haul her stuff from Texas to Tennessee. She claims Atlas damaged and lost her belongings en route, and sued in Texas state court for some 71 grand in damages.

Atlas removed the action to the U.S. District Court for the Southern District of Texas, and it appears Ms. Fraser-Nash, who represented herself in proceedings, somehow learned about the Carmack Amendment. The only problem was that she either had no evidence, or didn’t know how to show it to the court.

When Atlas moved for summary judgment, the court went through the elements of a Carmack claim, and the shipper failed each time. First, she couldn’t show her cargo was tendered in good order and condition. The Fifth Circuit has held that a bill of lading stating “apparent good order,” like Atlas’ did, is not sufficient proof of good condition when the shipper packs her own freight in packaged the carrier couldn’t inspect. In fact, some of this shipper’s freight had been stored in a bin four years before Atlas touched it. Fraser-Nash claimed most of her stuff was brand new, but provided no proof of that.

Second, Fraser-Nash also had no proof that some of her freight was lost, as she presented no evidence of inventory or otherwise to demonstrate just what was missing. In fact she hadn’t even opened all the delivered boxes to see what had been delivered.

Third, she had no proof of damages. Fraser-Nash didn’t name an expert or provide admissible evidence of any damaged items. You’ve gotta do better than that, and having a lawyer would be a great start.

## Hot Recent Cases (Continued)

**A carrier's limitation of liability defense fails on summary judgment: why carriers should make sure they issue proper documentation *before* the shipment.**

*Mid-American Energy Co. v. Start Enterprises, Inc.*, 2008 WL 391239 (S.D. Iowa 2008)

Carrier Start had hauled shipper Mid-American Energy's freight for some time. In this instance, Mid-American tendered to start a cargo of expensive computer equipment for shipment from Nebraska to Iowa. Apparently, a Start employee dropped the computer, didn't tell Mid-American's rep about it, and had him sign a bill of lading attesting to no damage. He signed the form in spaces for both point of origin and destination, and didn't read it before affixing his John Hancocks. No bill had been given to the shipper at time of tender.

When Mid-American discovered the damage, it sought damages from the carrier, and the two wound up in the Southern District of Iowa. Start wasted no time pointing to the limitation of liability clause in its bill of lading, the same one neatly signed in two places by Mid-American's unwitting rep.

The court analyzed each of those hoops a carrier must jump through to limit its liability. A couple such obstacles tripped the carrier up, i.e., the ones that say you have to issue a bill of lading at the time of shipment, and reasonably offer the shipper an option to purchase full liability. Having failed to do the former, Start couldn't realistically argue it had done the latter. Mid-American's signatures don't cut it under the circumstances, because they indisputably came after the fact.

**Underpayment claim tossed out based on *res judicata*.**

*H&H Brokerage, Inc. v. JR Simplot Co., Inc.*, 2008 WL 394998 (E.D. Ark. 2008)

This decision contains an interesting procedural analysis resulting in summary judgment dismissal of a transportation broker's claims against a shipper based on the doctrine of *res judicata*.

The relationship between a transportation broker and motor carrier - owned and operated by the same principals per a fairly typical transportation business structure - resulted in legal presumptions against the common interest.

Transportation broker H&H Brokerage and motor carrier H&H Transportation were sister companies. H&H Brokerage had a contract with shipper JR Simplot, for which H&H Transportation handled most shipments. When business slowed, JR Simplot entered into a new contract directly with H&H Transportation. Under the new agreement, JR Simplot agreed to pay freight charges pursuant to a rate sheet.

JR Simplot filed a lawsuit in the federal court for the District of Idaho in September 2005 against H&H Transportation seeking recovery for damaged freight. H&H Transportation counterclaimed for underpayment of certain charges under the second agreement. Apparently, the jury sided with H&H Transportation, and awarded it the underpaid freight charges.

Fast forward a couple of years, and H&H Brokerage sued JR Simplot in the Eastern District of Arkansas for allegedly unpaid freight charges. Going through a complex analysis of *res judicata*, collateral estoppel, and issue preclusion, the court ruled that H&H Brokerage's claims were compulsory counterclaims that H&H Transportation failed to interpose as part of its counterclaim in the Idaho action, and therefore were barred in Arkansas. The two companies are in privity - very close privity at that - and conducted business essentially as one entity.

If this decision isn't disturbed on appeal, it could create interesting issues for transportation companies who offer brokerage and carriage services under separate legal entities.

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