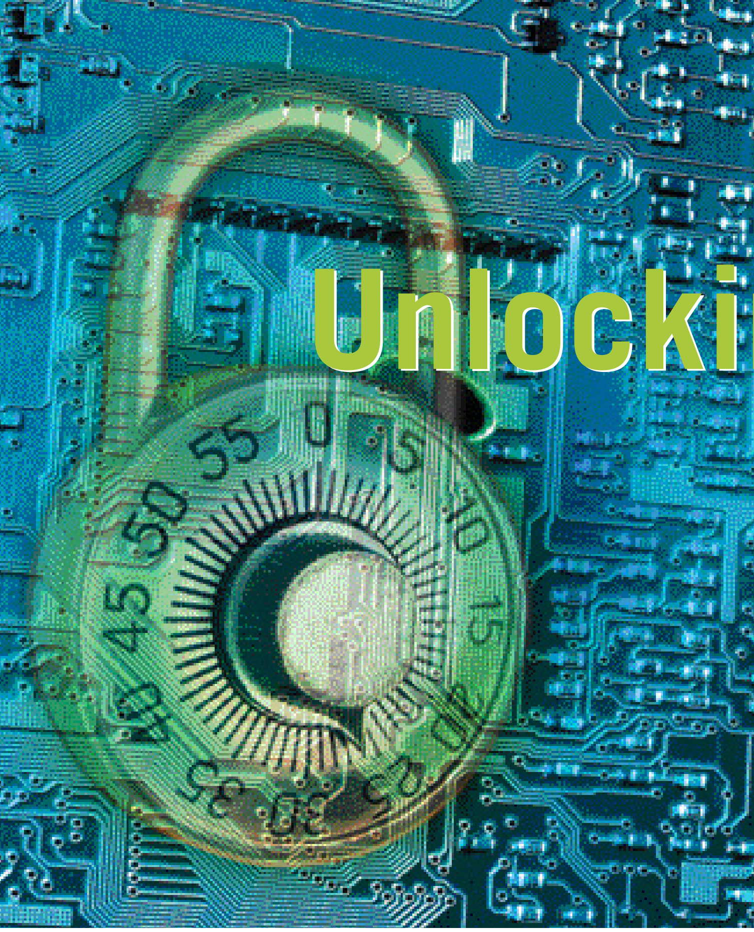

Unlocking the Clues
to the UPS Agreement

Not understanding your agreements can cost you!

— By Thomas Andersen —

Once upon a time, UPS would provide agreements to their customers that were simple to understand. They included a single discount for Ground, Air and Hundredweight services, while fees were relatively "easy" to predict. Those times have changed. Beyond being unfamiliar with UPS' discounting practices, most people now truly do not understand their agreements. Measuring the impact of the pricing in these agreements can be challenging to decipher, even for the most seasoned consultant.

Upon your completion of reading this, my hope is that this article will help you better understand how to measure the discounts and savings that are offered in the UPS agreement and position you to ensure that all applicable areas are addressed. There are also some recommendations and tips to ensure proper implementation of any new UPS pricing agreements.

The UPS Agreement

Whether it's a small to mid-sized business, National or Global account, more than 90% of UPS agreements are structured in a similar manner. It may be six pages or 36 pages, but structurally, most agreements are similar. Assuming that you have one of these "standard" agreements, the first page typically includes the term of the agreement (the standard is three years with a 30-day out clause that applies for either side to execute), date of expiration of the offer and general information that pertains to most UPS clients.

The next page of the agreement (or next few pages, depending on the number of account numbers) is typically titled Addendum A. It includes the account numbers and the applicable Commodity Tiers (not to be confused with the Portfolio Tier). The number that's stated next to the account number and address (if there is a number) reflects the Hundredweight Tier that would apply for that account (typically a specific location). Discounts and adjustments to minimums being excluded, Tier 1 reflects the best pricing, while Tier 7 contains the least aggressive pricing. In theory, the Commodity Tier is "commodity" driven. Lamp shades and light bulbs would theoretically fit the Tier 7 label, while bricks would fit the Tier 1 criteria. In reality, it's not that black and white.

Following that, we get into the meat of the agreement (typically labeled Addendum B). As this area gets a bit detailed, let's approach it in sections:

Although **fee adjustments** can be addressed in areas throughout the agreement, most common domestic fee adjustments are typically included near the top of this section. With more than 100 various fees that can be applied, it's unrealistic to get into details. An important and consistent factor, though, is the term of the fee adjustment. It's common practice to see reductions to fees being limited to 12 months. Keep an eye on this, and if the adjustment is nearing the end, proactively engage your UPS Account Manager to address it.

This is followed by the **guaranteed discounts** that are applied to Ground (weight-driven) and International (Import and Export — typically zone and/or country driven) services. These are discounts that apply whether a shipper is achieving a small portion of the volume commitment or exceeding the volume commitment substantially. That's not saying that UPS won't exercise its 30-day out clause and revise the pricing, but the Portfolio

Tier Incentive is in place to help manage this. There's more to come on the Portfolio Tier Incentive, shortly.

Any adjustments to the **standard dim weight factors** would also typically be included in this section. The dim divisor (194 Standard for Domestic and 166 for International Export) simply determines the dimensional weight, which is the size of the package in relation to its actual weight (rounded up to the next whole pound). As one would expect, the billable weight will be the greater of the dimensional weight and the actual weight.

For example, a 30-pound package measuring 24"x20"x16" would be billed at 40 pounds, based on the standard dim divisor of 194 being applied (7,680/194 = 39.6 pounds). There is a notable exception. For Ground shipments (not Air), if the cubic size of the package in inches is less than 5,184 (three cubic feet), UPS currently applies the actual weight of the package. Don't be surprised to see UPS change this in 2010 or in the coming years.

This then leads us to the **Portfolio Tier Incentive**. Additional incentives for Ground and International shipments, as well as the discounts for all applicable Domestic Air services, are included in this section. For Ground and International shipments, one simply adds the incentives in the Portfolio Tier to the discounts stated in prior sections. There's no math-magic here. I emphasize now, however, that if a specific service level is not stated, don't expect that it will be discounted. The default in the portfolio tier is to have a six-tiered structure, with the third tier traditionally representing the targeted discounts, based on the volume that UPS expects to be committed. It can range from two to six tiers, however, so determine what the current history is, prior to assuming that you qualify for certain discounts. This can be accomplished by asking your Account Manager for the historical volume (past 52 weeks' history) or by viewing your bill. The Gross Weekly Revenue can also typically be estimated by calculating the past 52 weeks' pre-discounted transportation charges, exclusive of any fees, divided by 52 weeks. If pricing has been implemented recently, the history may have been reset, so the applicable weeks would then need to be used for the calculation. UPS has ingeniously created this tiered structure that heavily penalizes a shipper that doesn't continue to commit close to 100% of its forecasted or historical volume. If there's growth, however, you'll typically find that there is only a slight incentive in the higher Tiers.

Adjustments to minimum charges, typically stated as a reduction off the Zone 2 (or applicable zone for International shipments) Letter or one-pound Tariff rate, are then provided towards the end of Addendum B. Minimum charges can have a substantial impact, so always consider this when comparing proposals, either between carriers or when comparing a new proposal versus the existing agreement.

Calculating True Savings

While calculating shipping costs was relatively easy a few years ago, shippers must now decipher the billable weight, dimensions, mileage (zone) between the origin and destination location, as well as the service level. The applicable service level is no longer limited to Commercial versus Residential, but rather if the shipment is a regular pickup, freight collect regular pickup, third-party regular pickup, undeliverable, freight collect undeliverable or third-party undeliverable. For air services, the AM option must also be considered, as well as the Hundredweight option that applies once multiple pieces combine to weigh more than 100 pounds. And yes, as stated previously, if the service level is not stated in the agreement, it is highly likely that an organization is paying the tariff rate for that shipment.

Also, note that discounts are applied only to the applicable service, whether it's a transportation charge or accessorial surcharge (fee). Don't combine the base transportation charge with applicable fees prior to discounting them. Instead, calculate each component separately (accounting for minimum charges) and then add them up. Make sure to include the fuel surcharge for each item since it applies not only to the transportation charge, but also select fees.

One other area to acknowledge is that there are minimum charges that can apply to all services — and typically do. Once applied, this can result in a significant offset to negotiated discounts. If a shipper sends primarily lightweight shipments or ships more regionally (zones 2-4) than nationally (zones 5-8), they will typically experience much lower savings than they may have anticipated.

Making Sense of it All

Rather than approaching this article by bundling all the carrier agreements into one, we chose to begin by providing our thoughts and insight to the UPS agreement. It is unquestionably the most complex and cumbersome to understand, and many of the components that apply to this agreement can be applied to other carrier agreements.

UPS is extremely good at what it does, and it offers a very good product and service. It has also been the most effective at structuring its agreements and implementing pricing that returns the greatest margins. UPS may claim that its complex pricing agreements were created in order to target the areas that impact the shipper the most. More realistically, it was created to help UPS maximize profits. This wasn't created by mistake. It was designed to make it challenging for shippers to manage and control, and for UPS to continuously improve profitability.

If you view your UPS agreement and it doesn't follow the structure listed and you have any questions, please feel free to contact me. Otherwise, I hope that this article has been of value to you. ■

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