

10 Ways to Reduce Fleet Costs

OPERATING A COST-EFFECTIVE AND EFFICIENT FLEET OFTEN REQUIRES RELYING ON THE KNOWLEDGE AND EXPERTISE OF FLEET MANAGERS, BUT STRATEGIC DIRECTION FROM UPPER MANAGEMENT ALSO ACTS AS A DRIVING FACTOR FOR SUCH CHANGES.

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Save



Establishing key performance indicators (KPI) derived from the fleet organization, vehicle assets, and vendors, permit effective fleet performance. This allows chief decision makers to observe trends as they evolve over time.

Here are 10 specific ways to reduce fleet costs along with ratings on each method's potential to affect the organization's overall profitability:

1. Reduce the Fleet's Size

Reducing the number of vehicles in any given fleet is the most proven way to reduce overall costs. The average total cost of ownership (TCO) for a light-duty vehicle (under 10,000-pounds GVWR) ranges from \$5,000 to \$8,000 per vehicle, per year. Eliminating 100 vehicles offers a potential savings opportunity of more than \$500,000 per year. While removing these vehicles would proportionately eliminate 100 percent of fixed costs, the likely increased workload required of the remaining fleet vehicles will raise the operating costs for those vehicles slightly; however, there will still be a net decrease in overall fleet operating costs.

The reduced savings amount will vary based on mileage and usage; however, results from Mercury Associates' studies show a reasonable expectation of 5 to 10 percent TCO reduction, although some clients have experienced savings as high as 15 percent.

Cost-Reduction Potential: Large

2. Cut Miles Traveled

The number of vehicle miles traveled is one area where fleet managers typically have limited, if any, control. Other than monitoring and enforcing personal-use policies, fleet managers are not privy to day-to-day business purpose data or have the tools to measure the reasonableness and justification for such use. Still, unnecessary trips with little business justification occur and such events drive up vehicle operating costs.

A practical solution involves greater involvement by supervisors in monitoring driver territories, business-use reports, and number of sales/service calls in relationship to mileage and time.

Also, take advantage of technology. With the interconnectivity of today's business environment, employees can utilize teleconferencing and various media communications to eliminate the need for physical travel. In addition, GPS and other telematics solutions not only reduce unnecessary mileage by providing improved routing, but also discourage excess usage that can occur when the driver believes "no one is looking." In fact, studies have shown that the mere notice (to employees) of mileage reporting audits have an impact that results in mileage reductions — across a range of business, personal, and reimbursement mileage — without incurring a significant investment cost.

Fleet managers should be tasked to work with driver management teams to implement practical solutions to reduce miles traveled and develop return on investment (ROI) analysis for use of telematics and other technology solutions.

Cost-Reduction Potential: Small to Moderate

3. Get More MPG

Federal government regulations have and will continue to greatly influence and impact vehicle size/weight and development of new automotive technologies. Current Corporate Average Fuel Economy (CAFE) standards of 27.3 mpg for passenger vehicles and light-duty trucks will increase to 35.5 mpg by 2016 and then rise again to 54.5 mpg by 2025. Automakers agreed to the 2025 measures, but there will be an interim assessment in 2017 to review both the cost and effectiveness of different approaches. Three strategies offer direct means for improving fuel economy and reducing fuel consumption:

1. Reduce vehicle size and weight. Vehicle downsizing and down-weighting will likely become a critical means of meeting CAFE requirements. As seen with the all-new, aluminum-body 2015 model-year Ford F-150, lightweight materials will play a bigger role and displace traditional materials such as cast iron and steel. Advanced high-strength steel, aluminum, composites, magnesium, and titanium will all be used more and more in automotive components.

Fleet managers are actively seeking to reduce vehicle size. To do so, they should invest time into better understanding the functional purposes of the vehicles that they manage. This requires spending time in the field, an undertaking that many fleet managers fail to do. Only by thoroughly understanding business requirements, can fleet managers begin to appropriately downsize vehicle models, downsize engines, and add suitable options while avoiding negatives such as mechanical failure and downtime.

2. Use Innovative Automotive Technologies. The use of existing engine technologies and the current demand for hybrids are expected to continue; however, while plug-in hybrids and electric vehicles improve fuel economy, higher acquisition costs rarely produce an ROI when using vehicle lifecycle principles. It appears these alt-fuel vehicles will continue to be a small percentage of overall vehicle production. Meanwhile, diesel engines, often regarded as the least "clean" vehicles on the market, have made advanced strides in greenhouse gas emissions and provide substantially better fuel economy than their gasoline counterparts.

Automakers are expected to accelerate their focus on engine improvements that can achieve a light-duty vehicle mileage

of 40 mpg. Replacing six-cylinder engines with four-cylinder engines equipped with a turbo or super charger also improves fuel economy, while not diminishing horsepower. Other engine changes that improve efficiency are 7- or 8-speed transmissions or continuous variable transmissions.

As a side note, a number of aftermarket vendors have developed and marketed various fuel additives and devices designed to improve mpg, however, many of these products fail to provide realized performance increases when tested in laboratory settings approved by the U.S. Environmental Protection Agency (EPA).

3. Modifying driver behavior. Many organizations with fleets fail to consider the impact drivers have on vehicle fuel economy. Hard acceleration, idling, inconsistent speeds, excess use of air conditioning, and hard braking are bad driver habits that can be corrected with driver training and/or education. According to the EPA, a driver can impact fuel efficiency as much as 33 percent. Such strategic direction, however, requires collaboration on all levels of management in order to achieve driver buy-in, acceptance, and success. Some vehicle tracking systems can also monitor and report "events" such as hard acceleration, braking, or cornering, and can also reveal excessive idling time. A business case analysis can determine whether investments in these technologies are warranted.

Cost-Reduction Potential: Moderate

4. Lower Fuel Cost

Fuel is often the second largest variable expense (after depreciation) faced by fleet managers. The U.S. Department of Energy (DOE) Energy Information Administration (EIA) expects the trend for 2014 is a continued drop in fuel cost. Fleet managers, however, should remain alert for potential spikes and keep a proactive fuel management program in place at all times. Practices such as acquiring fuel-efficient technologies, vehicles weight reductions, additional transmission gears (e.g., 8- to 10-speeds), and appropriate drive types to meet business needs should be continued even when fuel prices are stable.

While certain fleets have found savings in natural gas (NGV) or propane autogas, vehicles, implementing these alternative fuels often requires long-term strategic planning. Vehicle acquisition and/or upfitting costs can exceed \$10,000 per vehicle, although, recent technology improvements that have brought down the cost of NGVs to near-parity with diesel engines. Gas reserves have greatly expanded the supply and reduced the cost of natural gas. Other positive developments are increased vehicle availability (from OEMs) and the availability of support for fleet and infrastructure development.

Key NGV users include municipal fleets (e.g., refuse haulers), local utilities, state fleets, private fleets (e.g., taxis), airport shuttle buses, commercial urban delivery trucks, manufacturing facilities, transit buses, and farm-use vehicles. Studies support that the greatest savings opportunities exist with refuse and transit fleets, followed by other medium- and heavy-duty vehicle fleets such as school buses and other fixed route fleets (e.g., delivery). These fleets all share a common operational feature in that the vehicles return to a single location where they are time-filled overnight. Taxi fleets are similarly centralized.

Cost-Reduction Potential: Small

5. Reduce Lifecycle Costs

Senior-level executives may see frequent vehicle replacement as an unnecessary cost to the overall fleet budget, instead encouraging fleet managers to retain their vehicles until they reach an older asset age.

Mercury's studies have found that many organizations retain and operate vehicles far past their optimum economic life, which can result in excessive maintenance costs, increased fuel costs as the vehicles decrease in fuel economy, and reduced utilization. This practice of utilizing an aging fleet stems from previous practices, a lack of capital funding, or failure to communicate the costs and benefits of timely fleet replacement.

Reducing vehicle lifecycle cost requires the knowledge of how to optimize replacement cycles and conforming to the correct replacement cycles. Best-in-class fleet organizations utilize economic-based replacement planning tools to empirically determine the proper lifecycles for vehicle replacement.

After considering all relevant factors (e.g., initial new vehicle cost, reasonable projected resale value, fuel mpg, planned maintenance and projected repair, personal use payments), the fleet manager can prepare short and long-term replacement plans.

Cost-Reduction Potential: Moderate to Large.

6. Lower Acquisition Cost

The largest component of TCO is almost always the depreciation of any given asset. However, fuel may exceed depreciation for very high-mileage, low-acquisition cost fleets. At any rate, achieving the lowest vehicle acquisition cost possible is paramount to reducing fleet costs. Even fleet novices understand that the lowest acquisition cost is not necessarily the optimal vehicle to acquire because the resale value of the vehicle plays a pivotal role in TCO. For example, a subcompact sedan may cost less initially than a midsize sedan, but the sub-compact may depreciate more, resulting in a higher TCO.

Common acquisition cost-reduction strategies also include negotiating price based on "triple-net" cost. This means starting negotiation with the dealer (or lessor, who is acting as the buying dealer) at dealer invoice, exclusive of OEM factory holdback, flooring (e.g., OEM financing paid to the dealer), and advertising refunds.

Factory-paid dealer delivery fees should also be negotiated along with receipt of national fleet or retail incentives (whichever is lower). Once a transparent net price is established, the fleet manager should negotiate a reasonable flat fee of profit for the dealer.

Fleet organizations should also negotiate volume discounts with one or more OEMs, employing either a single or multiple OEM vendor strategy. These discounts vary widely and are not necessarily dependent on fleet size. Generally, fleet organizations that start negotiations early in the model year get the best opportunity of savings. An OEM most often offers the greatest incentives for the vehicle models that they wish to "move." This may be due to the phasing out of low-demand models or simply that the OEM has greater profit to share.

Regardless, savvy fleet managers employ lifecycle principles to determine the best deal, using reliable residual value projections from automotive industry resources such as ALG, Black Book, and others.

Note, ordering vehicles from the factory vs. out of dealer inventory saves, on average, at least \$1,000 (some calculate \$2,000) per typical light-duty vehicle. The target benchmark for out-of-stock acquisition is less than 1 percent.

Cost-Reduction Potential: Moderate to Large.

7. Assure Higher Resale Value

Previous sections of this article have dealt with the importance of managing depreciation and selling a vehicle at the economically optimal point in its lifecycle. Corporate fleets typically sell an average of 16 percent of its vehicles to employees (10 percent on the low end and more than 20 percent at the high end, depending on the industry). The advantages of driver/employee sales include:

- Faster receipt of proceeds.
- Higher residuals (priced a bit higher than wholesale).
- Driver takes better care of the vehicle.
- Auction and transportation fee savings.

Fleet managers should have mechanisms in place to prevent drivers from spending for unnecessary cosmetic, non-safety related repairs. Otherwise, true savings can be greatly diminished.

Additional ways to increase the resale value is to select only vehicle colors that yield the best return (typically white and other neutral colors) and to provide maintenance records to potential buyers. Reducing the cost of sales improves net residual gains. Thus, avoid any reconditioning of the vehicle other than moderate cleaning (less than \$80). Managing auction and transportation fees can reduce the cost of sale by hundreds of dollars.

Finally, fleet managers should benchmark sales results against reliable fleet industry publications such as Black Book "fair" condition.

Cost-Reduction Potential: Small to Moderate.

8. Lower Maintenance Costs

Often, fleet managers adhere to outmoded beliefs for preventive maintenance (PM) practices, such as the belief that a PM should be performed every 3,000 miles. Such frequent PMs are only required for vehicles that operate under "severe" duty as defined by the OEM. Executive decision makers should consult with their fleet managers to determine the ideal practices for the company's fleet, using OEM recommendations as a resource. Many light-duty fleet intervals have been extended to between 6,000 and 7,000 miles. Increased use of synthetic oils will also extend PM intervals (offsetting the higher cost of synthetic oil). Thus, on-time PMs become more important as intervals between PMs are extended.

After many years of ongoing price increases, tire costs were stable in 2013, largely as a result of pricing wars between the tire companies that brought down prices. A significant factor influencing tire cost has been the increased diameters of OEM-specified tires. These larger tires, however, increase mpg, vehicle performance, and have a longer tread life, which will likely mitigate increased tire cost.

Cost-Reduction Potential: Small to Moderate

9. Lower Crash Costs

The safe operation of employer-provided and employee-provided vehicles is of paramount importance in a well-run fleet organization. An effective safety management program provides many benefits that have a direct impact on profitability:

- Reducing the risk and cost of accidents and injuries.
- Reducing the cost of insurance.
- Increasing driver productivity.
- Enhancing driver morale and retention.

A commonly used methodology to translate crash costs into lost profits is to take the fully loaded expenses associated with fleet crashes and divide the number by the organization's operating profit margin. The result is the total additional sales revenue the organization must produce to replace lost profits due to fleet crashes. For example, in an organization with an operating profit margin of 10 percent and annual accident-related expenses of \$500,000, an additional \$5 million in sales revenue is needed to replace the \$500,000 in lost profits due to accidents.

Fleet managers alone cannot implement and sustain a successful safety program. It must be driven from the top and be a CEO and COO priority, as well as being actively supported at all levels of management.

Finally, sources such as Risk Management magazine and Risk & Insurance Online provide ample examples of court punitive awards due to fleet accidents that tally into the millions:

- 2007: Florida, \$11 million settlement.
- 2004: Georgia, \$2.75 million jury award.
- 2004: Texas, \$3.5 million settlement.

Cost-Reduction Potential: Moderate to Large

10. Lower Overhead Costs

Overhead costs, also known as indirect costs, include the cost of management and administrative staff, buildings and facilities, including fuel sites, computer systems, utilities, tools, taxes, and many other factors that cannot be attributed directly to a vehicle. While no set formula exists for calculating the percentage of a fleet budget devoted to overhead, an Activity Based Costing (ABC) exercise is useful for identifying the sources of these costs as a first step.

Cost-Reduction Potential: Small to Moderate.

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