

# Which 3PL is right for you?

As we see it, the 3PL business is booming. Every day a company decides a third-party logistics services provider should take on the complex and costly job of distributing its products because it wants:

- To focus on product development or business acquisition or anything other than distribution and logistics
- The flexibility of responding quickly to changing business volumes
- To avoid the upfront expenditures for a distribution building, equipment and technology, and staff

No matter what the reason you are seeking a 3PL, you should never outsource what you don't understand. Before you begin the interviewing and selection process, thoroughly examine and document every part of your current operations if there is one. If none, do your research.

## Do the Math

You should understand all costs involved in outsourcing compared with in-house fulfillment. You will have to calculate each of the costs involved in providing your own services, from call center to personalization to fulfillment to invoicing to managing returns. Building lease or construction, material handling equipment, warehouse management system, and direct and indirect labor expenses also must be included in your calculations.

With calculations in hand, you'll be prepared to interview potential 3PLs in order to develop an apples-to-apples comparison of their services and costs with your own. Narrow your choices down to a handful and set up meetings with each of them.

## Points to Consider

**1. Common measurement unit** – It is confusing to compare costs when 3PLs price their services in different units. For example, put-away could be priced by pallet, while replenishment is by carton, and gift-wrapping by hourly labor. In order to compare their costs with yours, you will have to convert quotes for the different services into a common measurement unit, usually per piece or per order. The time and effort to develop a comparison matrix is well spent.

**2. Savings in freight costs are possible** – A 3PL might receive a more favorable per shipment rate than you would be able to achieve due to multiple customer purchasing power and shipment consolidation opportunities. You can expect to pay roughly 5% to 8% of overall net sales for shipping.

In today's multi-carrier environment, a 3PL should be expert in choosing the right carrier for your shipments. Find out which carriers are chosen and why. Ask about their use of consolidators that are part of the USPS Parcel Select Program to reduce costs.

**3. Initial implementation cost** – 3PLs often charge an up-front fixed cost based on the complexity of the service. This cost is for planning and development of material handling, operational and information systems required for the distribution operation and implementation of the proposed system.

Some 3PLs may also bill for the time needed to calculate your charges.

**4. Fixed and variable fees** – Distribution costs are calculated using a fixed and variable fee structure. Fixed fees are charged monthly

or quarterly, irrespective of the number of orders shipped. Variable fees are charged per hour, per item or per order for each distribution function such as receiving, putaway, pick-pack-ship, customization, customization, inspection, returns processing, etc.

All costs should be clearly identified. As a rule of thumb, total distribution cost per unit should be no more than 8-10% of the product's sales value, without shipping costs.

**5. Facility and information systems infrastructure** – It is extremely important to scrutinize facility operations, material handling equipment, and information system infrastructure, since they indicate ability to deliver in a timely and accurate manner. Comprehensive information system architecture can provide you with real time inventory data, as well as status of the order.

Be sure to decide what level of sophistication is necessary to handle your products so you do not pay for more than you need. Then plan to be present in the facility on a regular basis to maintain visibility of the infrastructure.

**6. Location of fulfillment centers** – No matter what the 3PL charges for order fulfillment, you will be responsible for freight costs to ship customer orders and to receive goods from suppliers. The location of the 3PL's facility or facilities must enable reaching maximum customer population in the shortest amount of time with minimal shipping cost.

**7. Flexibility to accommodate sales surges** – Seasonal businesses should partner with a 3PL which has the resources to meet its sales volume surges. A 3PL should be able to explain in detail how it will modify its operations to suit your sales cycles and growth – in a manner that will maximize customer service. Ask the 3PL for references from businesses similar to yours.

**8. Operations efficiency** – In most distribution operations, labor costs are billed on a per hour basis. The most efficient 3PL operations should be the least costly. By adding your work to its operations, a 3PL should reduce its overall costs per unit. It might offer to share the realized savings with you.

**9. Minimum commitment** – Since a 3PL will make some changes to its operations with the

addition of your business, you should expect a minimum time commitment to be included in the contractual agreement. Make sure the length of time fits with your business plan, especially if you plan to develop your own operations in a shorter period than the 3PL has in mind. No matter how the contract period is defined, you need to understand the penalties for breaking the contract or not meeting the minimum commitment.

If your start-up business plans to develop its own distribution operations in the future, begin creating your "exit plan" before signing any agreement.

**10. Customer service level** - It is most important that a 3PL meets your customers' requirements for time between order and delivery. Make sure you and the 3PL are using the same measurement. Look at all the details of customer service, such as sample orders.

**11. Your management team and business plan** – 3PLs are eager to partner with companies which come to the table with an experienced management team, a strong financial history or backing from well-established venture capitalists, and ambitious yet realistic business plans and projections. Arriving prepared for your first meeting with a 3PL puts you in a position of strength and provides greater leverage in negotiating contractual terms and agreements.

## **The Final Result: Customer Delight**

The fact that you are using a 3PL should be transparent to your customer. No matter whether you choose a 3PL, continue your current operation or develop a new operation from scratch, remember the importance of an efficiently run business.

You can give away the task of providing the service, but never give away your ultimate responsibility for it. Know the people responsible for managing your distribution. Plan to make regular visits to watch your product move, as long as it's in the hands of a 3PL.

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