Logistics consultant **Gideon Hillman FCILT MIC** looks at how businesses can successfully outsource their logistics operations, highlighting the significant do's and don'ts that can make or break the relationship.

The third way

The range of services being offered by today's Third Party Logistics Providers (3PLs) are increasingly extensive as the highly competitive market drives development and innovation.

3PL contracts now regularly expand beyond the traditional warehouse and distribution activities, and have evolved to incorporate customer call centres,

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procurement, assembly operations and even production. However, the overall benefits of the 3PL service offering have remained the same; they provide the expertise, specialist resources, and asset investment that will enable you to focus efforts, and capital, on the core business.

The increasing number of 3PLs in the market, the range of services offered, and the ever-increasing pressure for businesses to reduce costs, is facilitating significant growth in the contracting of 3PL services. As this growth continues, it is ever more important for potential clients to properly consider how 3PL services are engaged, and what the 3PL will deliver.

To select the best 3PL for your business, and maintain a mutually beneficial relationship, you need to ensure that the appropriate service is selected in the first place. There are many cases where relationships have broken down between the 3PL and client, due to expectations of either one or both parties not being managed from the outset. The erosion of the relationship can start as early as the initial meetings, where the service requirements are first established.

For example, in February 2010 a High Court judgement ruled against the service provider in the case of BSkyB Ltd v. HP Enterprise Services Ltd. Whilst this case relates to an IT project (not a 3PL contract) there are aspects of the case which need to be borne in mind by those involved in any aspect of pre-contractual discussions for service provision.

In its judgement, the court was particularly critical of the way in which the supplier's proposal had estimated resource required to undertake the project; specifically, the approach of giving a deliverable which the customer was seeking (as opposed to properly determining the extent of effort required).

The court's decision confirmed that it is not possible to exclude, or limit liability, for a fraudulent misrepresentation made during the sales process; and that no subsequent contract clause could be engaged to prevent a claim for that misrepresentation. Whilst not new law, this judgement has reinforced the importance, for service providers, to act within the confines of what they are able to deliver. It also underlines the need for those service providers to undertake appropriate due-diligence, ensuring that the service they are offering is not only deliverable, but is fully consistent with their client's requirements.

Mitigate risks, identify benefits

Sometimes, 'misrepresentation' from a service provider can be a reflection of the client not fully assessing their exact requirements and therefore the services they need. To mitigate this risk, you need to both fully analyse your businesses requirements, and ascertain how you will integrate with the service provider. Both of these things need to be completed well in advance of initial discussions with a 3PL.

Where logistics services are being procured, clients should be prepared to undertake an internal supply chain review, developing a full understanding of their logistics and service level requirements, and identify all potential benefits within a well-structured business case. This business case will provide the prospective 3PLs with an appropriate requirement specification; in turn, this specification will assist the 3PLs to design a solution that meets the client's actual needs.

Making the right choice

The next step is to choose the right 3PLs, which should always be undertaken through a managed and well structured tender process. Tendering is not just to establish cost competitiveness, but it also helps clients measure and establish the culture fit, and the operational capabilities of the 3PLs. It is also important to establish that the 3PL not only meets immediate requirements, but also has the ability to provide for your business growth expectations, and the desire for continuous improvement.

The tender process should also not be restricted to the 'big five' 3PLs. Quite recently I managed the tender process for a major automotive OEM, who wanted to outsource their global freight and landside consolidation logistics operations. Despite the size and complexity of their requirements, I still identified over 30 potential providers in the pre-tender qualification process. Many of those providers were small 3PLs that had formed strategic business partnerships to broaden their foot-print.

This, in conjunction with the advanced and centralised IT systems as well as working to a standard set of operating procedures, meant they were able to provide seamless international multi-modal networks – traditionally the preserve of the major 3PLs.

In addition, the smaller provider is often more willing and able to give a bespoke service tailored to the client's specific needs. This is in comparison with the 'standard' service often provided by larger 3PLs who often have a fixed and less flexible infrastructure already in place.

The tender process should also allow the service provider to be innovative. For example, you should not be prescriptive in demanding that the network has to be 100% dedicated without assessing the potential for shared-user operations.

Many 3PLs can now leverage significant economies of scale through shared user networks, thus allowing you to access facilities at lower operational costs. The key factor within the shared use facilities is that the costs are transparent for you to ensure you are only paying for the agreed warehouse space and service that you use.

Retendering

It is also worth considering that many companies retender their outsourced logistics operations at the end of the contract term. In reality the market place and service capabilities of the 3PLs will probably have changed over the current contract term, and my experience shows that just retendering the same operation can provide cost savings in the region of 8 to 10% of annual spend, but that the potential savings are far greater.

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For example, Wales & West Utilities logistics contract renewal in 2009/10, provided the opportunity to completely review the existing logistics strategy and gain significant advantages throughout the supply chain, rather than just reduce the costs of the current outsourced 'Hub & Spoke' operation. The tender process completely changed the logistics strategy already in place, and resulted in significant annual cost savings far in excess of what would have been achieved through re-tendering the already established hub and spoke logistics operation.

Summary

In final summary, any business who plans to engage a 3PL, needs to firstly invest the effort to properly define a business case and service level expectations, and follow a properly managed tender process. Not only will this facilitate better savings, but it will also provide a better platform for maintaining a mutually beneficial relationship with the chosen 3PL throughout the contract term.

It should also be noted that the management of the 3PL/client relationship is a joint responsibility, and the process for regular review and service measurement must be clearly established within the service level agreements (a key part of the contract).

It is misguided to sign a 3PL contract and just let the 3PL get on with the job without any regular interaction from you. If, as is likely the case, your business is dependent on the correct functioning of your logistics operation, then you should always work closely with your chosen 3PL. ●

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