

Improving Unsaleables Management Business Practices

Joint Industry Recommendations

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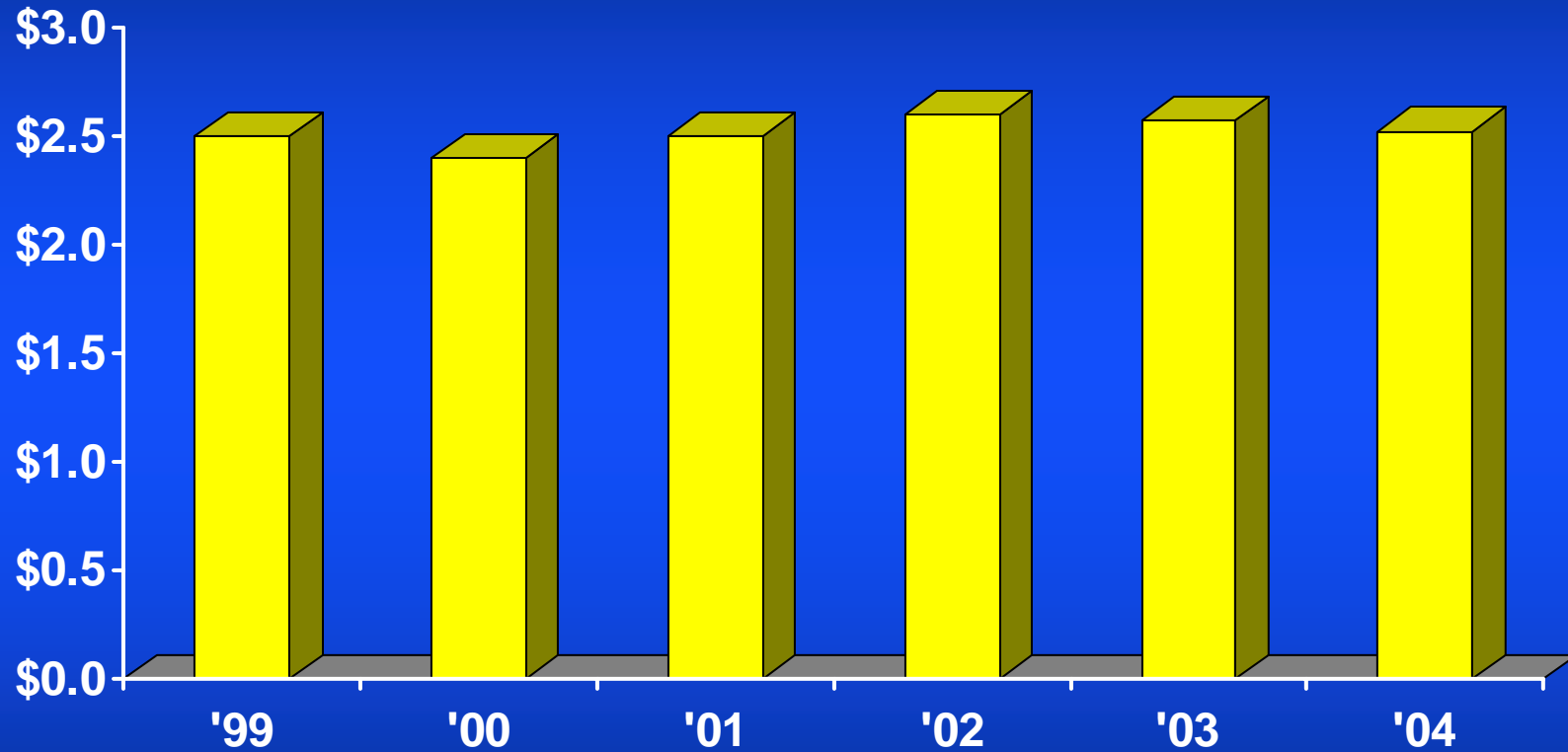
Background

FMI and GMA directors recognized current discord in the industry.

- **Some manufacturers and distributors believe that some trading partners do not behave fairly regarding unsaleables.**
- **Each side wants the other side to be fair.**
- **Sales agents and wholesalers find it especially difficult to collaborate with trading partners to control unsaleables costs.**

FMI and GMA directors concerned about steadily rising levels of unsaleables costs.

Annual Cost of Unsaleables (*\$Billions*)



Background

- **Unsaleables Leadership Task Force formed in January 2005 from Joint Industry Unsaleables Steering Committee.**
- **Developed a new set of industry business practice guidelines for unsaleables product management and cost recovery.**
- **Based on the 1990 JIR guidelines and principles.**
- **Inclusive of changes that have occurred since 1990.**
- **Published recommendations in November.**
- **Released at FMI Mid-winter Conference, January 2006.**

Unsaleables Leadership Task Force

Albertson's, Inc.
Bozzuto's Inc.
Campbell Soup Co.
Coca-Cola North America
ConAgra Foods
CVS Corporation
Food Lion, LLC
General Mills, Inc.
Gerber Products Company
The Gillette Co.
Hannaford Bros. Co.
Harris Teeter, Inc.
HEB Grocery Co.
H.J. Heinz Company
Kellogg Company

Kimberly-Clark Corporation
Kraft Foods Inc.
Land O' Lakes
Nash Finch Company
Nestlé Purina PetCare Co.
Nestlé USA
Pharmavite Corporation
The Procter & Gamble Company
Rite Aid Corporation
S.C. Johnson & Son, Inc.
Safeway, Inc.
SUPERVALU Inc.
Unilever Bestfoods N.A.
Wakefern Food Corp.
Walgreen Co.
Winn-Dixie Stores, Inc.

Existing guidelines were published in 1990 in a report sponsored by six associations titled “Product Reclamation Centers: A Joint Industry Report” (JIR).

Since then:

- **Several industry conditions have changed.**
- **Fundamental reason for the industry’s interest remains – the existence of damaged, expired and otherwise unsaleables products in the supply chain.**

1990 Joint Industry Report

Product Reclamation Centers: A Joint Industry Report (“JIR”)

- A set of **recommendations for fair and equitable business practices** for manufacturers, sales agents and distributors in dealing with unsaleables.
- A **study of the handling and operating costs** of a typical product reclamation center.
- Consensus of 1990 Joint Industry Reclaim Center Committee – 32 members, wide industry representation from 6 associations

Cost study was not revisited by 2005 Task Force.

Industry Changes Since 1990

- Some manufacturers pay from non-JIR “adjustable rates” or “swell allowances” which are derived and applied differently across companies.
- Most companies have unsaleables policies, resulting in conflict when trading partners have different policies.
- Most reclaim centers are now operated by outside companies. Most were operated by retailers or wholesalers in 1990.
- Facilities have consolidated and now process more efficiently.

Industry Changes Since 1990 (cont'd)

- Deductions are now used more often for claims and payments.
- Service companies process claims for some manufacturers and may be part of deduction authorization process. Service companies pick up for some manufacturers at reclamation centers.
- Salvage revenue is significant for some retailers and some manufacturers.
- New Bioterrorism Act recordkeeping requirements cover reclamation centers and exclude food banks.
- Environmental regulations for landfills are more stringent now.

Task Force Group Consensus Process

- FMI, GMA and consultant facilitated project.
- Nature of the JIR Task Force and volatility of issues prevented 100% agreement on many statements and recommendations.
- They agreed to allow the group consensus to prevail over individual company positions.
- Some representatives respectfully disagreed with the general consensus of the group.



Task Force Focus



- Develop new recommendations for issues not covered by JIR.
- Preserve common goal of reducing quantity of unsaleables in supply chain.
- Improve efficiencies of dealing with unsaleables.

2005 Task Force Conclusions

- Reclamation centers are currently the most efficient way to remove unsaleable products from the supply chain
- The negative implications to the supply chain if all reclamation centers ceased operations outweigh the positive implications.
- The reclamation center industry is in a consolidation phase which will likely result in fewer processing facilities.
- As long as unsaleables continue to exist in the supply chain, trading partners should deal with them in a responsible, fair and efficient manner.

2005 Task Force Recommendations

- Individual trading partners should continue to use the voluntary guidelines and tools published in the 1990 “JIR” for efficient product reclamation.
- Industry leaders should consider the current role and implications of reclamation centers during top-to-top dialogues.
- Individual manufacturers should consider both unsaleables policy methods – the JIR and the adjustable rate policy (ARP) methods.
- All unsaleable products should be processed through reclamation centers.

2005 Task Force Recommendations (Cont'd)

- **Manufacturers and distributors should collaborate on efforts to reduce the quantity of unsaleables to mitigate some of the conflict around unsaleables.**
- **Trading partners should adopt a mission of total cost reduction in addition to cost recovery in discussions that involve reimbursement for unsaleables costs.**
- **Trading partners should use product condition data.**
- **Reclamation centers should be used for the efficient consolidation and control of non-damaged product where mutually agreed-upon by trading partners.**
- **See report for more...**

Key Attributes of an ARP

- 1. Based on statistically sound data that measure performance of manufacturer's products throughout entire supply chain. Data are used to:**
 - Define opportunities for improvements.
 - Establish the rates that the manufacturer uses to compensate customers for unsaleables.
- 2. Measurement process should be ongoing and be the basis for periodic adjustments to the compensation rates.**
- 3. Address all causes of and responsibility for unsaleables.**
- 4. Commitment to continuous improvement.**

Topics to Reference in an ARP

Topic	Cost Owner	Process Owner
Manufacturer-caused	Manufacturer	Manufacturer
Warehouse-caused	Retailer/Wholesaler	Retailer/Wholesaler
Consumer-caused	Shared	Retailer
Store-caused	Retailer	Retailer
Expired Products	Shared	Shared
Handling Fees	Shared	Retailer/Wholesaler

Additional Topics That Should Be Discussed

- Trading partners determine an exit strategy and extraordinary situations handled outside of an ARP.
 - Manufacturer discontinued/withdrawn
 - Distributor discontinued
 - Seasonal products
 - Promotional products, special packs, shippers
 - Underperforming new product/category launches
 - Product transition
- Topics deal with residual inventory or excessive damages.

Dynamic Process for Developing Unsaleables ARP

1. *Develop product data base*

- Logically group products into business units or categories.
 - Package type and cube package & case.
 - Category variations.
 - Shipping platform types.
 - Distribution modes.
 - Total shelf life in days.
 - Minimum days of shelf life remaining at time of shipment.
- Log dynamic data into the database
 - Volume data by business units / categories by channel.
 - Inventory turns data by business units / categories by channel.

Dynamic Process for Developing Unsaleables ARP

2. Map physical supply chain flow including:

- All processes
- All touch points
- Measurement points for the audit
- Production facilities through reclamation centers
- All points in between
- Each type of order selection & retail distribution methodology (may be channel specific)
- Map the data transfer processes related to the physical flow of goods
- Identify all processes within the supply chain map where product and package performance is potentially impacted by the processes.

Dynamic Process for Developing Unsaleables ARP

3. *Develop a statistically valid supply chain audit sample and schedule* taking into account:

- **Calendar cycles** – Audit in all months of the year
- **Customer channels** – Audit in all channels in which the manufacturer does business in proportion to channel share of business
- **Regionality** – Audit in all geographic regions in which the manufacturer does business in proportion to the region share of business
- Include manufacturer shipping points in audit

4. *Conduct the initial audit* using qualified internal or external resources

- Collect data in archivable and accessible format

5. *Calculate the rate(s)*

Dynamic Process for Maintaining Unsaleables ARP

1. Review baseline steps 1-3 and make changes where necessary due to all dynamics of the business including:

- New item introductions.
- Product discontinuations.
- Brand and company mergers, acquisitions and divestitures.
- Customer mergers and acquisitions.
- Market share changes.

2. Conduct the update audit using qualified internal or external resources

- Collect data in archivable and accessible format

3. Calculate the rate(s)

Types of Rate Applications

- ***A national average*** applied to all customers
- ***A channel average*** calculated for each of the manufacturer's customer channels
- ***A geographic average*** calculated for each major marketing area in which the manufacturer does business

Important Considerations for Manufacturers

- **Decision about components in Adjustable Rate Policy requires extensive analysis.**
- **Company should be able to consistently measure and retain accurate data relevant to:**
 - Individual components of the ARP
 - How it conducts business with trading partners
- **The Unsaleables Leadership Task Force recommends a continuous process for determining the reimbursement rate NOT a one time calculation that remains in place for years.**

Closing Thoughts

- The Unsaleables Leadership Task Force strongly recommends **open dialogue** about non-confidential details regarding the development of the adjustable rate
- Manufacturer sales representatives or agencies should have **adequate documentation** describing audit and rate calculation methodologies
- The Task Force encourages retailers and wholesalers to provide **open access** to reclamation centers, stores and warehouses for the purpose of investigating causes of unsaleables
- When manufacturer **policy changes result in a payment shift**, the inventory and unsaleables that reside in the retailer and wholesaler supply chains at the time of the policy change also need to be addressed

Any questions?



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