



## The 13 Steps to a Successful Retail Vendor Compliance Program



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## TIME TO PLAN

### Retail vendor compliance is a complicated, and at times controversial subject...

Controversial obviously because consumer goods manufacturers are generally not happy about paying penalties for non-performance – even if well deserved – and there is no question that there have been examples of retailers running programs that appear abusive to some suppliers.

When this happens, vendors view compliance programs as fundamentally unfair, perceiving the “chargebacks” to be at times arbitrary, often not clear, and set at overly high levels.

That can give vendor compliance programs a bad name even for those retailers that are doing it the right way. *SCDigest* believes that vendor compliance programs run the right way can be identified by several key attributes:

- A focus on improving supply chain and logistics performance, not generating chargeback revenue
- Programs and penalty regimens that are easy to understand, with prompt and clear communication of errors and penalties when they occur
- Chargeback levels that accurately reflect the cost to the retailer from the error

Gough Grubbs, Senior VP of Logistics and Distribution at Stage Stores, offered this wise perspective on a videocast on the Supply Chain Television Channel several years ago: “I just put it to vendors this way: We have a contract that details what and how you are going to deliver. When you deviate from that contract, when you don’t deliver what you promised, we incur some costs that need to be recovered.”

... Controversial obviously because consumer goods manufacturers are generally not happy about paying a penalties for non-performance — even if well-deserved.

## The Benefits of Vendor Compliance

Retail vendor compliance programs really should be considered as falling under the broader category of vendor performance management, a structure many leading retailers have already embraced.

Within that context, retailers are trying to address a wide range of supply chain and logistics problems through vendor compliance.

The chart below was taken from a survey *SCDigest* performed on customers of Traverse Systems, a provider of compliance management and vendor performance management solutions, asking those retailers what problems they were trying to solve with their compliance programs (“*The Value of Retail Vendor Compliance Optimization Technology*”).

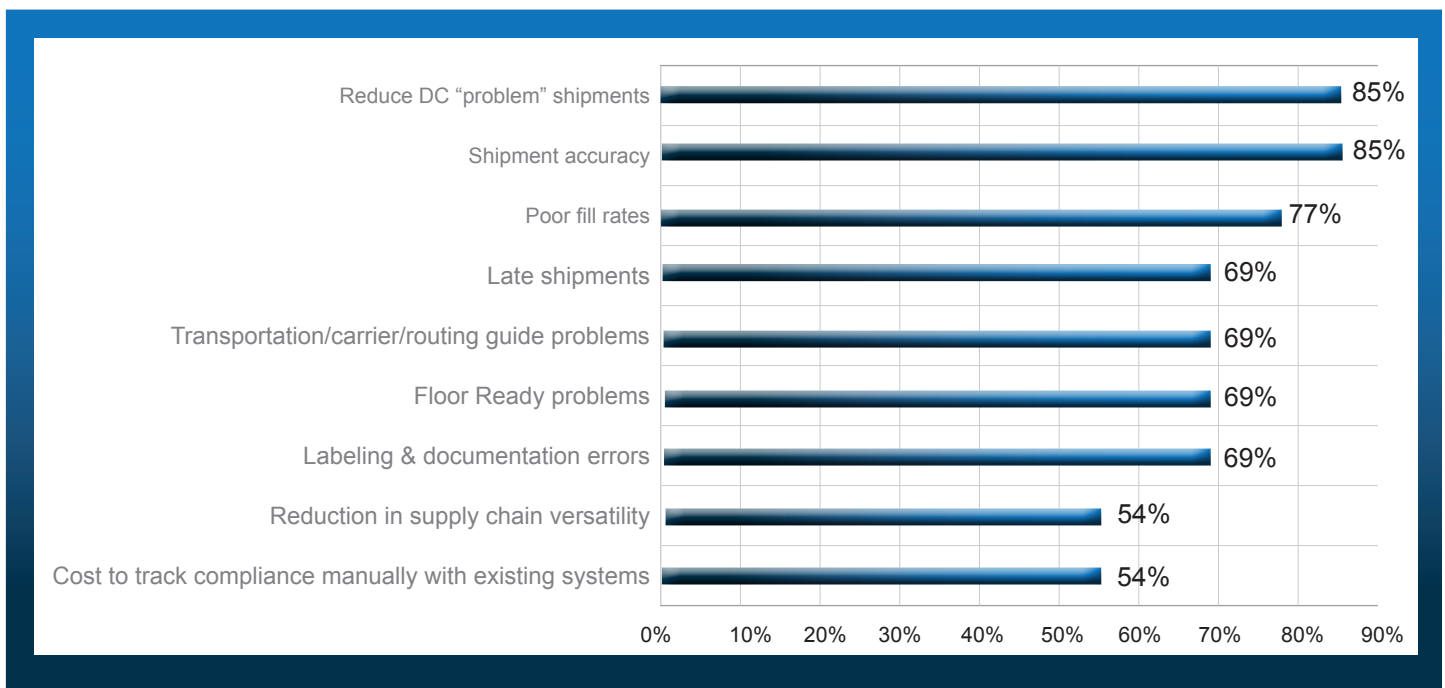
As can be seen, the top two problems being addressed were “reduction of DC ‘problem’ shipments” and improved “shipment accuracy,” each cited by 85% of respondents. Right behind that, at 77%, were “poor fill rates,” but in fact all the problem areas listed were called out by more than 50% of survey respondents,

illustrating the potential of compliance management to improve supply chain performance.

On another *Supply Chain Television Channel* videocast, Camille Fratanduono, VP of Inventory Planning & Replenishment at auto parts retailer Pep Boys, made this comment relative to the value of vendor compliance programs and technology (Traverse Systems): at their company: “Our compliance program is clearly delivering measurable results in terms of improved vendor performance, which enhances our supply chain effectiveness.” So the value of vendor compliance management seems clear and demonstrable – if it is done right. The reality, however, is that the scope and effectiveness of vendor compliance programs varies widely.

The efforts of literally hundreds of retailers over many years has certainly shed some light on what the keys are to compliance management program success. We distilled 13 – a baker’s dozen – of those guidelines here in this white paper, which we present in the following section.

### What Problems Were You Trying to Solve with Compliance Optimization Software?



# #1

## Start with the End in Mind

It may sound obvious, but it is critical that there is a clear vision about the role and results from a vendor compliance program at the outset of the effort. And that vision needs to be developed across several functions within the company: distribution, transportation, finance, merchandising, etc.

Too often compliance programs are initiated in one area, say distribution, with a vision and scope that does not adequately accommodate the opportunity for these other functions. Or, it comes from a sort of knee-jerk reaction to some pressing issue – e.g., reducing the number of “problem” shipments – and thus does not take a broader view of all the potential benefits of a successful program.

What are the real goals of the program? Is it in the end primarily about chargeback revenue, or is the focus to improve supply chain performance and wring out costly errors over time? Is compliance an opportunity to gain competitive advantage? How will areas outside the supply chain, notably merchandising, benefit from the program?

These are among the key questions that must be answered early on so that there is a clear vision and set of objectives to guide the program’s design and success criteria.

# #2


## Assemble the Team



A basic and obvious step, forming the team that will drive the program needs to be tackled early on, and per the discussion above needs to be truly cross-functional: distribution, transportation, IT, finance, merchandising/sourcing, etc.

Many retailers of course have a “vendor relations” group, and this is the natural place from which the vendor compliance effort should be led. But there is a big difference between having such a group leading the process and receiving input from other areas and actually forming the type of cross-functional team discussed above.

Not only is the program scope and impact likely to be enhanced from the more inclusive approach to the team, it will get early buy-in from these other functions as they see ways to address some of their own interests and challenges, something much harder to achieve later if they were not part of the process from the beginning.



“What are the real goals of the program? Is it in the end primarily about chargeback revenue, or is the focus to improve supply chain performance and wring out costly errors over time?”

### #3

## Benchmark Other Compliance Programs

Since hundreds of retailers have gone down this path, why not learn from their efforts and mistakes?

Retailers (as with other companies) are at times reluctant it seems to reach out to their peers for such insight, even though such benchmarking efforts can save a company looking at a compliance program much effort and help them benefit from the “lessons learned” of these established programs.

Of course, direct competitors are not likely to offer a benchmark opportunity, but the number of retailers

doing vendor compliance is so broad, across so many different sectors, that finding non-competitive retailers really should not be much of a problem.

If you are talking with providers of compliance management technology, they will often have their own insights into program design that will be useful, but more importantly likely can connect you to some of their existing customers who would be willing to share their experiences, recommendations, and lessons learned.

## Define Success Metrics & Requirements

### #4

How will the company know in the end if its program is a success?

The team must define what metrics will be used to judge the program, and what level of achievement is expected over what time horizons.

This of course gets back to the first point, as to what goals and opportunities are really driving the compliance initiative. What areas of supply chain improvement are expected to be improved, and by how much (problem shipments, fill rates, lead times, routing guide compliance, etc.)?

Clearly, there will be expectations set relative to cost recovery via chargebacks for vendor errors, but will

this decline over time as performance improves? Not enough retailers really grapple and resolve these questions.

Once the target metrics are defined, likely in a time-phased way, now a retailer must identify the changes in people, process and technology needed to deliver those promised results.

This of course is an iterative process, since decisions on technology support (to pick the most obvious area) likely will impact what can really be achieved. But the net result of this step is basically the development of the plan: what is expected to be achieved from the compliance program, and how the retailer is going to get there.



*...By reaching out to industry peers, benchmarking efforts can save a company a lot of effort while gathering insight from “lessons learned”...*

# #5

## Develop Vendor Requirements

What specific vendor requirements are you going to monitor? Will they all be released at once, or phased in over time? Will the requirements apply to all vendors, or will different categories of merchandise have different requirements?

Of course, this is an area where something like omni-channel adds some complexity. For example, if some vendors will be drop shipping to customers for some on-line orders, what will be the new requirements for this kind of relationship, and how will performance be monitored?

Retailers should not underestimate the time it will take to assemble these requirements, though again this is an area where benchmarking may be quite helpful. Many existing compliance requirement documents are readily available over the internet, or can be easily accessed by calling a given retailer and asking for a copy.

While such a review can provide some great insights into what the rules should be, avoid “cut and paste” syndrome – the rules should be your own, not some other retailer’s, who may or may not have done a good job with their rules.

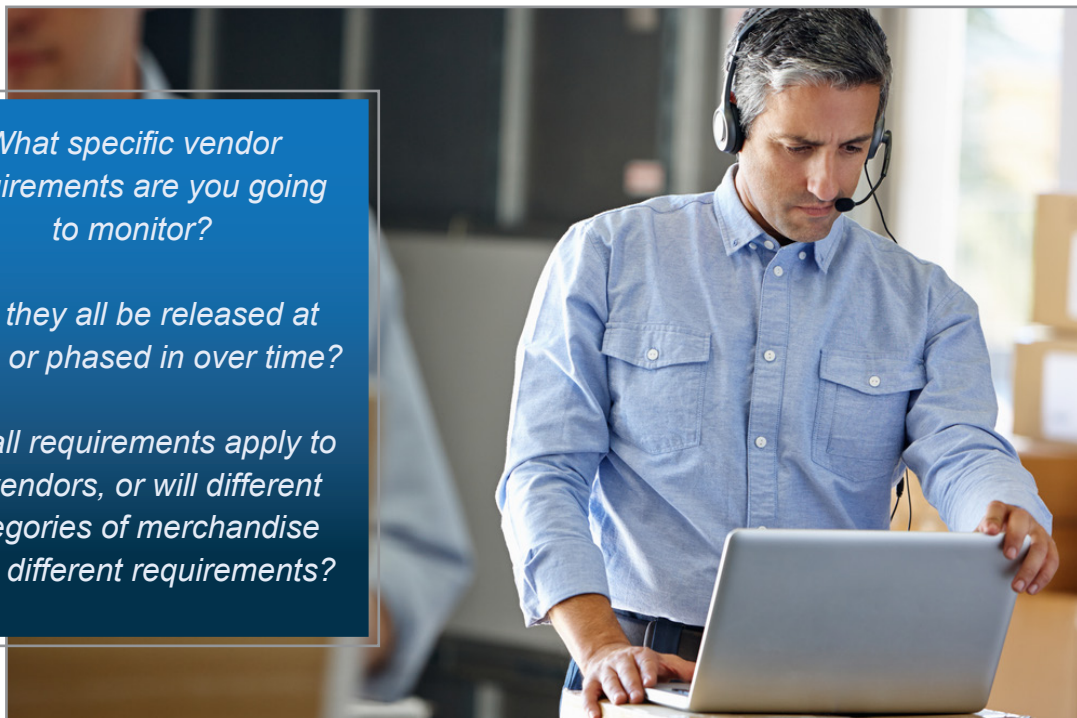
We would also highly recommend sharing the emerging requirements before their release with leading vendors. Some of the requirements could cause vendor issues that you had not foreseen, and/or the vendors may have experiences with other retailers that offer a better approach in some areas.

While retail vendors may not be thrilled with the idea of another compliance program and certainly with the possibility of new chargebacks, they would still prefer to have an opportunity to comment on the rules before they are released, rather than after the fact.

*What specific vendor requirements are you going to monitor?*

*Will they all be released at once, or phased in over time?*

*Will all requirements apply to all vendors, or will different categories of merchandise have different requirements?*



For many reasons, it is really impossible to enact a quality retail vendor compliance program without a strong level of technology support.

Think of what a compliance management system must do:

- It must be capable of receiving and integrating data feeds from numerous sources (EDI communications, PO systems, warehouse systems, transportation systems, etc.)
- It must be able to store all this data in a data warehouse-like structure and be able to cross link all this information (e.g., here is what the ASN said versus what was actually received)
- It must provide some way for DC workers to enter information about errors in shipments, including pictures of problems, such as with labeling/ticketing
- It must be able to communicate with vendors relative to deficiencies, hopefully in a very timely and detailed manner
- It must be able to calculate the appropriate chargebacks and electronically send those to the retailer's financial systems

And those are only the “must haves.” Other technical capabilities related to vendor compliance include: the

ability to produce vendor “scorecards”; using all this data to provide improved supply chain visibility (e.g., to the “PO lifecycle”); providing portals to vendors through which they can monitor their performance chargeback history, and more.

All told, that's a lot of technology. Many retailers decide right upfront to use a third-party solution as the foundation of their programs. For others, it's a make or buy decision, and many have in fact opted for homegrown solutions.

While there is no one clear right answer, we believe history has shown that retailers going the homegrown route often stall in their efforts, as continued IT support just isn't available. It is also extremely rare for homegrown systems to have anywhere near the breadth of functionality that commercial solutions (many now available in the Cloud) can provide today right out of the box.

As noted above, what the technology can do becomes a critical question not only to answer that part of the full program, but because the technical functionality will define and constrain what can be achieved in terms of program scope and results.

### Key Capabilities of an Effective Compliance Management System

1. Receive and integrate data feeds from numerous sources
2. Store all data in a data warehouse-like structure, cross link all data
3. Provide system for DC workers to enter information and related pictures about errors in shipments, etc.
4. Communicate deficiencies with vendors quickly and efficiently
5. Calculate appropriate chargebacks and electronically forward to retailer's financial systems





## #7

### Think Through the Approach to Penalties & Scorecarding

Will the program include chargebacks, or will the data only be used to develop vendor scorecards that will be used to influence vendor performance? Most but not all programs, it must be noted, involve chargebacks, though hybrid chargeback-scorecard programs are increasingly popular, especially among retailers looking to use compliance mostly to improve supply chain performance.

If there will be chargebacks, how will they be set, and at what level for each type of violation? There are no real rules for this, so each retailer must make these decisions on their own. However, *SCDigest* believes that at their core chargebacks should in fact be directly related to the cost to the retailer from the error. Charging more than that is unfair and will breed vendor dissatisfaction.

So, that means there is some hard work to do to estimate the real cost of different types of vendor

errors. Such estimates do not need to be perfect, but they should be defensible internally, and to vendors.

That said, Greg Holder, CEO of *Traverse Systems*,

recommends that retailers put themselves about in the middle of the pack when it comes to charges for different types of violations. If you come in too high, Holder says, it breeds the type of resentment and distrust discussed

above. More interestingly, if the penalties are set too low, a vendor may decide, for example, to late ship that retailer's order, because the penalty will be far less than it would be charged by another retailer, which therefore gets the merchandise on-time.

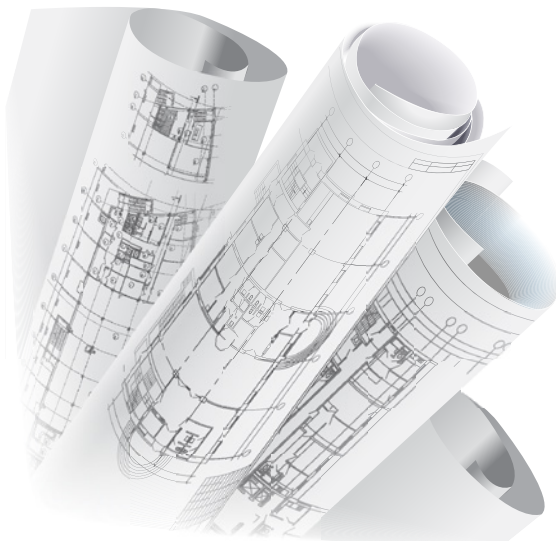
*SCDigest* believes chargebacks should be directly related to the cost to the retailer from the error... charging more is unfair and breeds dissatisfaction.

### Develop the Master Plan

## #8

Clearly, someone needs to take all this and develop a master plan for the program itself and its rollout.

That means a formal document is needed that lays out all key elements: overall objectives; detailed goals;



people, process and technology; time-phased plans and rollout dates; communication and education programs, etc.

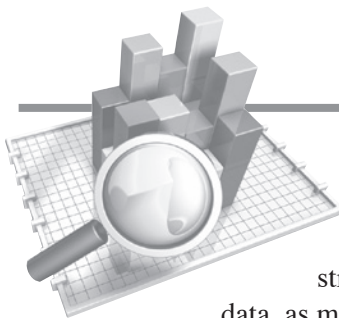
*SCDigest* research has found two common flaws in such retailer master planning: (1) failure to really layout a true multi-year plan beyond the initial program scope; and (2) failure to look at how all this data can be further leveraged to improve both vendor and retailer performance. There are many opportunities there, including visibility and analytics.

Of course, both points relate back to the fundamental issue of whether the vendor compliance program is primarily designed to deliver chargeback revenue or to improve the retailer's supply chain performance, a decision every retailer has to make for itself.

While vendor education is of course extremely important, as we'll discuss shortly, some retailers do not put enough emphasis on educating/training internal staff, from DC workers to managers and even merchants and executives.

As with any new initiative, people will make or break the program's success, and so many staff members need to be trained, not just on the technical workings of the system, but what the goals and objectives of the program are, and how this will help the company better achieve its overall objectives.

Front line employees who in many cases will be actually identifying vendor errors need to be especially well trained, as false error coding will quickly cause issues with vendors and lead to suspicion on every violation. It is smart to design the program such that it can catch any false positives or at least prevent as many as possible.



A vendor compliance program is only as strong as its underlying data, as many retailers have painfully learned over the years. That means that before launching a program a retailer must ensure the data being used for identifying violations and errors is rock solid.

There are of course really two types of data errors that could cause problems: (1) the raw data itself has issues (e.g., when a vendor shipment really arrived); and (2) calculations done among data elements

*“Don’t assume program benefits... are clear to all.*

*For example, It may be helpful to walk even manager-level staff through [for example], the process to reduce fill rate or how lead-time variabilities can reduce inventory levels.”*

Staff members that will be fielding vendor calls relative to the program also need to be especially well trained, and that training needs to be thought through. These folks need to have a working knowledge, not only of the distribution process but also general knowledge about vendor operations and the merchandising plan. What is the proper approach to dealing with a vendor which feels a violation is not accurate, or that a chargeback is unfairly high?

These are the kinds of questions and issues where again benchmarking with other retailers may prove quite valuable, as well as seeking the advice of any technology supplier you may be using who may have experience in dozens of these programs.

Don't assume that the benefits of the program, especially those related to supply chain improvement, are clear to all. You may need to walk even manager-level staff members through how reducing fill rate or lead-time variability can lead to reduced inventory levels, for example.

## Invest in Data Validation

(e.g., when did the shipment arrive in relation to the deadline for arrival).

When programs are launched with data quality issues, they quickly lose all credibility with vendors from which it may take years to recover. In addition, it will place great stress on many staff members, from vendor relations to IT, who are constantly battling to sort out fact from fiction.

Achieving data quality is not easy, cheap or fast, but solid investment here will pay healthy dividends down the road.

# #11

## Develop an On-Board Strategy & High Quality Materials for Vendors

Of course, a detailed plan for how the program will be rolled out to vendors is required. Similarly, an approach must be defined for new vendors as to how to get them on the program.

In general, most retailers seem to launch their programs for all vendors simultaneously, but doing so in waves by region, type of size or vendor, or other attribute is certainly worth considering.

Simply sending out the new compliance rules and penalty levels is of course not nearly enough – though some have gone with this approach! Retailers should invest in high quality materials across a number of different media (e.g., documents, video, web), and likely should hold live on-line events to explain the program to vendors (and it wouldn't hurt to have internal staff listen in as well.).

*SCDigest* also recommends testing these materials with a small subset of vendors first before rolling them out to the full vendor community. It is almost certain that the test group of vendors will make

suggestions that improve the material's clarity and value.

**Be realistic about roll-out schedules... IT work, such as requiring Advance Ship Notices, typically requires months of preparation to ensure processes are working correctly.**

Also, retailers must intelligently assess just how much time is needed for vendors to prepare for meeting the requirements. Anything involving IT work, such as requiring Advance Ship Notices (ASNs) for the first time, is going to take the vendors a lot of time (months) and require a lot of testing on both sides to make sure everything is working. Be realistic about roll-out schedules.

## Assemble a Special Support Team for Roll-Out

# #12

During the early months, calls, complaints, issues, etc. will likely be very high in the first six months of a roll-out, even if the program and materials have been very well designed. At some point, the vendor interaction will slow to some reasonable and manageable level, especially if your system does a good job documenting and communicating errors and violations (e.g., timely communication, with details and photos as appropriate). The lack of such timely

and detailed information is consistently one of the biggest complaints by manufacturers around retail compliance programs.

Whether that team can be assembled from existing staff is a question you will have to answer, but bringing in a small group of well-trained temp workers for a few months is certainly an option worth considering.

But in a new program, it is important that vendors feel they can have timely access to managers to get their questions answered or better understand specific violations – especially since in a new program, there are certainly times when the vendor might likely be right about a chargeback not being correct.

*"Calls, complaints, issues, etc. will likely be very high in the first 6 months of a roll-out, even if the program and materials have been very well designed."*

Planning Quarterly Reviews of progress, issues, and opportunities may sound basic, but many retailers don't really do a good job of consistent reviews of their programs once they are first launched.

So, from the get-go a series of quarterly reviews of progress against goals, issues with the program, opportunities for additional improvement (e.g., beginning a vendor scorecard program), and more should be scheduled and attended by key stakeholders.

After the first year or two, the frequency of these review meetings can be ramped back a bit, say to once every six months, and maybe even eventually once per year. But early on, it is important to keep

a cross functional team well involved in how the program is advancing. This is especially true of course if different phases of the program rollout over some period of time.

The main point is that the expectation should be set that these quarterly reviews will be held for some period of time, with a cross-functional team, and that this process is a key element of a successful programs that meets its objectives.

*"The expectation should be set that quarterly reviews will be held with a cross-functional team. This process is a key element of a successful program that meets its objectives."*

## Seize the Vendor Performance Management Opportunity

How can reducing errors and variability from a retailer's supply base not be a good thing for its overall supply chain performance?

This is the mindset retail leaders have with regard to the compliance aspect of vendor performance management. It is a key weapon in the war to gain competitive market advantage through supply chain excellence, reducing costs, keeping stores shelves better filled, and having better service with lower inventory levels.

But the reality is the initial and on-going success of these programs vary widely across retailers. The

"troubled" programs generally arrived at that state from getting off to a bad start. Another key issue is not being crystal clear about goals for the program, across multiple functions.

Following these 13 tips for compliance program success will go a long way toward getting the program off to a very strong start and setting the foundation for long-term success.

*We wish you well in your journey.*

## = About Supply Chain Digest

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