

## **Chapter 15**

### **The A, B, C's of Building a Successful “Co-Packer” Relationship**

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#### **Overview on Using Contract Manufacturers or “Co-Packers”**

When natural and organic products began to experience double digit growth in a slow economy, manufacturers took note. Successful early co-packing relationships were often collaborations between the brand and the co-packer. This chapter will address the often unique needs of the natural or organic products in the traditional contract manufacturing model as well as review best practices when using contract manufacturers.

As the natural products industry grows, the need for quality co-packers who “get-it” becomes more urgent. With their emphasis on culture, value and generally higher price points, natural and organic brands must meet or exceed customer expectations. This can be challenging for a traditional contract manufacturer – where speed, efficiency and lowest cost are the driving factors in the relationship and tolerance for “mistakes” (read quality assurance) is higher. Just as natural/ organic products used to be considered “alternatives, there are alternatives for standard co-packing that can not only help achieve the financial, marketing and altruistic goals of the brand, but can enhance them.

Getting a contract manufacturer excited about your brand, your mission, and the product is a very worthwhile investment of your time. Traditional manufacturers need to be introduced to the unique aspects of the natural/ organic trade and be educated about the opportunity. Align the contract manufacturer with your own goals.

#### **What is co-packing?**

In business, co-packing and contract manufacturing are used interchangeably with the same meaning: production is outsourced to an entity other than your business. The best relationships have very clear

expectations from both parties, which ensure not only quality work but also as a basis for resolving any disputes that may arise. Contract manufacturing agreements range from informal verbal agreements (if you have an extremely high comfort level) to multi-paged legal documents which detail all anticipated eventualities. Often, smaller companies, or start-ups, have less formal arrangements with their chosen co-packer in an effort to help define the parameters that will later be used in a more binding agreement.

### **Why co-pack?**

Three very simple reasons, among many others:

1. Save your money. No costly investment in equipment, personnel, and infrastructure.
2. Free you up to concentrate on your own core competencies- sales, marketing, product design
1. This is the “core competency” of the co-packer...this is what they do... they are the experts.

Essentially, you are redeploying financial and management resources away from plant, equipment, labor and manufacturing overhead and putting your primary focus on sales, marketing and product development.

With the right co-packing agreement, you can decrease costs and potentially lower the expenses of raw materials purchases and carrying costs. This can reduce, *although rarely eliminates*, the need for inside operations and raw material management.

Below are two links to websites from contract manufacturing organizations that speak best to the advantages of co-packing. Review the information on these websites to determine if this route will help your business reach its goals. These resources not only answer the “why co-pack”, but can help you identify potential partners.

- [www.contractpackaging.org/](http://www.contractpackaging.org/) this website is a portal into your industry. Use it to locate co-packers in your industry, to access trade publications online (many of which can be read online), and to identify trade show
- <http://www.contract-packaging.net/>

Having already identified similar products in the marketplace you can narrow your search to your product category. Every industry has its own unique trade shows and trade publications. Here are a few reputable ones:

[www.Dmoz.org/business](http://www.Dmoz.org/business)

[www.Thomasnet.com](http://www.Thomasnet.com)

### **Consider Sheltered Workshops**

Sheltered workshops: This may be the solution to your short term or seasonal needs or for special pack sizes. These enterprises are looking for business opportunities and provide meaningful employment to people with special needs and/or circumstances.

Most sheltered workshops are assemblers and many have shrink wrap equipment

Sheltered workshops can be great solution for assembly of parts. Major metropolitan areas and smaller cities generally have these resources.

- [www.NISH.org](http://www.NISH.org) then link to “Community Rehab Programs” (CRP) for state lists
- contact your state’s Dept of Human Services

## Identifying and finding a good co-packer

Before approaching a contract manufacturer, either directly or through a broker or consultant, you will need as much information about your product as possible.

- Analyze your product and all its parts.
- Consider flexibility – can some parts be repacked for new items, club stores, multipacks?
- Know your costs: capturing the true cost of components includes the cost to get it to your door as a raw material or to the door of your co-packer.
- Cost of goods – know the bracket pricing for raw materials and packaging for each product
- Freight: cost to arrive at assembly point (your garage or your chosen co-packer) Use zip codes to determine.

*All the major shippers, USPS, UPS, Fedex, DHL have online quote Most major LTL firms (less than truckload – for palletized shipments) also have online quotes. The best LTL quotes will come from a firm you already have a relationship with. If your components are palletized for shipment, know the freight class of that component and any special requirements – refrigerated, frozen, air-ride (for fragile items such as glass).*

- Product specifications- written for each product
  - raw materials,
  - packaging specifications for raw materials and finished goods
  - lot coding information and preferred location
  - UPC and SKU numbers
  - Ingredient statements, nutrition facts panels
  - Allergens checklist
- Unique requirements (organic certification, kosher certification – hard to source ingredients)
- Retail price point and current cost of goods

- Seasonality
- Anticipated annual needs by unit and case
- Tolerance for substitutions – on ingredients, packaging. Pick up samples of what you like and don't like about potential substitutions

*NB: There is no reason to share your costs with potential co-packers. Ask them to quote given the guidelines you have provided. You can compare the cost and its effect on your gross margin.*

**Create a checklist of questions** to ask potential co-packers when exploring opportunities. The checklist should include any specific and unique requirements of your product

- minimum production runs
- frequency of runs
- lead times
- equipment capabilities and restraints(glass or plastic or both; carton dimensions)
- do they co-pack similar products? A good co-packer will protect the confidentiality of its current customers by addressing how they can meet your needs
- Turnkey or assembly: depending on the size of the facility, assembly may be the only option. Turnkey means that the co-packer will purchase all parts and sell a finished product to you. The more you know about your parts, the easier it will be to analyze the cost benefits to you for a either option or a combination (co-packer purchases corrugate and other materials, you provide raw materials) . Don't forget to consider your cash flow requirements !
- How do they handle receipt of materials and inventory ( you will require faxed or hard copies or all receipts signed and timed)
- Quality assurance: what kind of program is currently in place (in-house or contracted out) and will it meet your needs? Does your product require outside testing? QC Hold period length?

- Location, location, location – how will shipping finished goods to your distribution point affect the cost of goods?
- Production reports and technological capabilities; are day-to day operations people able to furnish reports, in what format and is that information useful to you in that format or will it require adjustments at either end?
- Third party inspections: does the plant undergo regular third party inspections? By whom?

### **Confidentiality Agreement**

Prepare a confidentiality agreement that should be signed by both parties prior to sharing any information , especially costs and suppliers. This is for your own protection while you search for the right partner. A simple one-two page can be drafted by your attorney, or purchased nominally on such sites as <http://www.ilrg.com/forms/confidagree.html>

### **Approaching contract manufacturers:**

While finding a co-packer can be as simple as a phone call from one of the trade organizations listed above, you may be better served by using the services of a consultant in your industry or type of product or working with a contract manufacturing broker.

- Consultants or contract manufacturing brokers: this is often the quickest route to legitimate source. This broker will generally negotiate his fee with the co-packer and that cost will be rolled into the quote to you. The broker is motivated to find an appropriate co-packer because ongoing business is the bread and butter. A good broker can create opportunity for your business that might not be available without the introduction.

- Word of mouth. Ask questions of everyone- your raw material suppliers, your packaging supplier, distributors, warehouses, truckers. Business runs on relationships- start building some of your own!
- Trade shows, especially packaging specific shows, can be an excellent resource. Ask questions!
- Private Label Show – this is a worthwhile investment if you want to locate the “players” in contract packaging

[www.plma.com](http://www.plma.com) Private Label Manufacturers Association

- Trade publications: the classified sections suddenly become more interesting

### **Co-Packing Agreements**

Co-packing agreements can be as simple (and binding) as a handshake, or a lengthy legal document. The product specifications are the foundation of the understanding between parties. These will create the parameters for quality control and assurance and your customer service. The product specifications are also used to define the most efficient and cost effective purchasing decisions (contract manufacturers can often leverage buying power for packaging and other materials). Your final cost will be affected by these decisions so carefully consider the advantages and drawbacks. Product specifications can be built on a template provided by the co-packer or jointly designed. It is essential that both parties agree to the specifications. Each change should be signed off by both parties and dated.

#### **Items to consider:**

- Raw materials or parts purchasing responsibilities
- payment terms
- additional services - QC/QA, product development
- negotiating shrink and other variables

- annual volumes, by units, by \$\$\$. May also include clauses for price reductions when certain volumes or dollar sales are exceeded within an specific time period
- minimum production runs
- changeover fees: these address the costs associated with shutting down a line to change materials or packaging. Contract packers like long continuous runs of the same thing because they are the most efficient use of materials, equipment and manpower.
- Shrink or loss percentages:
  - When setting up the specifications, create a tolerance, usually a plus/minus percentage for each part. The packaging agreement may specify that anything above the agreed upon loss for materials will be compensated.
- Production scheduling: determine lead time required for setting schedules and when it will be finalized. This may be as far ahead as 8 weeks prior to when finished goods are needed for sales or as quickly as the day before.
- Production reporting: as low tech as a fax of each production shift to daily electronic reports. Larger contract manufacturers have software specific to manufacturing so the reports should be modified to give you good information. This is also how to track loss in production that exceeds your expectations. Good controls at both ends of the relationship will aid in any “conflict resolution”.
- New equipment or customization expenditures. These may be dealt with outside of an agreement but should always be documented in writing. Negotiations may be on units produced or fixed time period and cost may be rolled into your toll charge (the cost to produce your product).

### **Handling disputes**

Stuff happens. Equipment failures, delayed shipments of materials/ parts, out of stocks.

As is the case in all relationships, good, clear, regular communication is the best diffuser of potential conflict. Manage expectations with clear information, preferably in writing (monthly production forecasts, reduces potential flash points). Seek out solutions to problems that are acceptable to both parties. Discuss your expectations. Responsibility for resolving defective materials issues or timeliness rests with the purchaser.



### **The Perfect Co-Packer...**

There are countless successful, thriving businesses that have grown without ever owning or operating a production plant. The “perfect” co-packer anticipates and plans for your success, has solutions for your problems, ideas for your promotions and is watching out for your best interests, if only because this is in their best interest as well. Many companies have multiple co-packers for different products or product lines (boxes and cans, glass and plastic). Each relationship stands in its own.

### **Organic certification and the contract manufacturer**

Good contract manufacturers already have quality assurance systems in place. Organic certification is another third party process. The co-packer may have organic certification in place, either for the entire plant, or only specific products and brands. If your product requires a certified plant, be sure you understand what you need because the process can be time consuming –certifying a plant from scratch can take as long as 3-6 months, or longer if appropriate systems are not in place.

Current copies of organic certificates for all your parts

Current copies of organic certificates for your product and brand

You may want to consider getting a co-packer certified under your company to produce only your items.

Discuss the process with your organic certifier.

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