

RIGGED

SUPERMARKET SHELVES FOR SALE



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CSPI and the Nutrition Policy Project

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Table of Contents

Executive Summary	i
Introduction	1
Why It Matters.....	7
A Tilted Playing Field	7
Location, Location, Location	9
How We Got Here	18
A Land of Giants	18
A Shift in Power	20
Putting Big Food’s Interests First.....	20
Lock Up a Space	22
How Food Manufacturers’ Payments Affect the Consumer Experience	24
The Two Million Dollar Entry Fee	24
Endcaps, Shippers, and Pedestals.....	29
Trade Spend	31
The Bottom Line on Fees.....	33
“Within an Arm’s Reach of Desire”	34
The System and the Little Guy.....	36
Other Retail Stores	39
Placement Fees and Convenience Stores.....	39
Food Sales inside Non-Food Stores	41
Policy Recommendations.....	42
References.....	45

Executive Summary

Supermarkets are so familiar that it's easy to take their design for granted. Begin with produce, shop meat and dairy along the perimeter, and end at a candy display by the register. Pyramids of soda 12-packs celebrate the upcoming game. Bakery scents waft throughout the store. But why do nearly all American supermarket chains generally follow the same layout, offer the same products, and use the same display techniques? Is it because this is what American customers want?

In part, but consumer demand is not the only force that drives what supermarkets sell.

Backroom deals between stores and food manufacturers also shape today's supermarket. In this world of wheeling and dealing, what customers want often takes a back seat to corporate contracts. Payments that food manufacturers make to retailers influence which products are offered and how they are displayed. Ultimately, those placements help drive what people buy.

Companies spend billions of dollars so that their products are featured and promoted in as many places as possible and in the most attention-getting places in supermarkets, influencing what people purchase and eat. First are the steep "slotting fees" that stores regularly assess manufacturers seeking to introduce a new product into the market. Perhaps a company has developed a lower-sodium version of a popular snack food. That innovator would need to come up with at least several hundred thousand dollars, if not \$1 million or more, to introduce that new item in all stores of the country's largest grocery chains.

For many categories of food, the payments do not end there. Supermarkets often charge manufacturers an additional placement fee as an annual rent for a spot in a freezer case or on a shelf. Those fees, or the equivalent in free product, can add up to hundreds of thousands of dollars in payments each year. That may be the cost of doing business to the multinational giants, but fees that steep can pose an impossible barrier for small companies.



These cardboard displays (“shippers”) allow Nabisco and Kellogg’s to get their products in front of customers who skip the cookie and cereal aisles. Their placement near the dairy case suggests that customers buying milk should also buy cookies and cereal.

The checkout aisle is typically the most expensive real estate in a store. There, a manufacturer can expect to pay a large supermarket chain as much as \$1 million a year to place a single product on the shelf. Then there are the lucrative “endcaps” (end-of-aisle displays) and “shippers” (cardboard displays) that the big grocery chains offer food manufacturers like items on a menu. A single “event”—a few weeks featured on an endcap or on a shipper—at a single large chain could cost in excess of \$50,000. All of these options add up to “360 Degree Marketing” for the biggest food companies, as a former marketing executive at Coca-Cola called it.

A spot inside a store’s weekly circular (also for sale) is out-of-reach to many companies. Then there are the billions of dollars that food manufacturers collectively spend on seasonal promotions (buy-one, get-one-free sales; 20-percent-off deals; and the like) that retailers typically demand of their suppliers. The ability to pay those “trade fees” represent another critical advantage that the food industry’s largest players have over smaller companies.

All told, supermarkets collect more than \$50 billion a year in trade fees and discounts from food and beverage companies, according to a group of academics headed by Gregory T. Gundlach, a marketing professor at the University of North Florida. As a result, the food system is rigged against everyone but the big food manufacturers with big marketing budgets, which tend to be the

most established companies and brands.

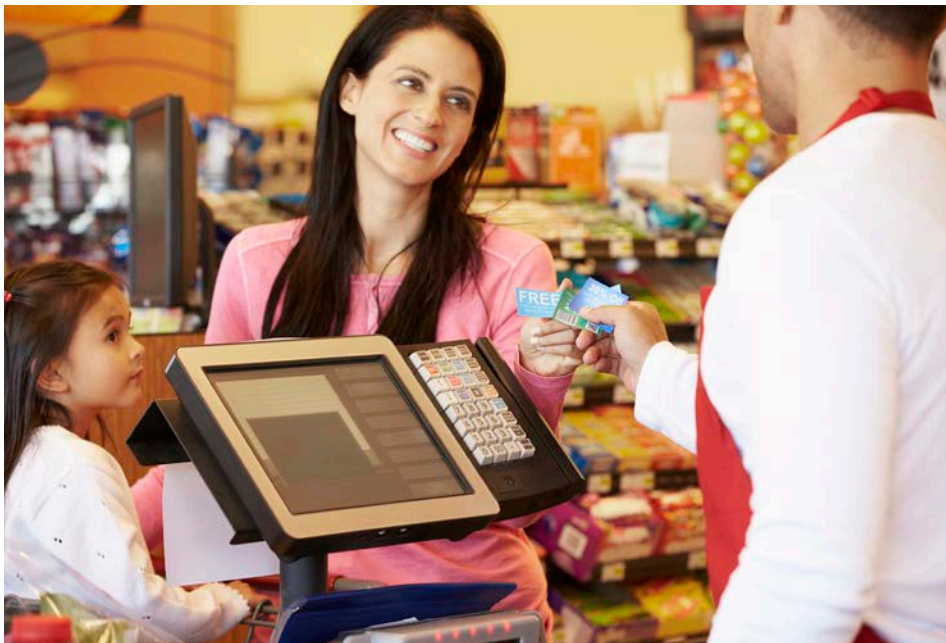
These fees matter. Fees are a key driver of which products are available to shoppers, how prominently they are displayed in the store, and how they are promoted, including through price discounts and specials. Putting products at checkout or on displays at the end of an aisle boosts sales significantly. It is obvious to customers that a business has paid for the giant billboard they passed on the way to the store. But many people have no idea that candy companies pay to put their products next to the cash register.

Another element of the modern-day grocery store is the “category captain.” In this bizarre system, a grocery store lets one big food manufacturer decide the entire layout of a section of the store that it already dominates, such as snack foods or soft drinks. One insider put it this way: category captains determine “everything from where and how products are shelved in supermarkets to how much of a product the supermarket should buy to whether a competitor’s product should see the light of day at all.”

To address this hidden manipulation of the marketplace, we recommend:

- The Federal Trade Commission (FTC) should investigate the use of placement fees in the retail grocery industry, assessing changes to the industry since its last look at slotting fees in the early 2000s and using its subpoena power to provide a more complete picture of retail placement fees.
- The Securities and Exchange Commission (SEC) should determine whether disclosure of trade-promotion practices should be required for publicly traded companies.
- State attorneys general should investigate whether the use of placement fees or the deference given to category captains violates antitrust or consumer protection laws and prosecute supermarkets whose practices illegally harm small businesses or consumers.
- Cities and counties should adopt healthy-checkout ordinances to ensure that the prime real estate of checkout is not used to undermine customers’ diets.

- Retailers and manufacturers should adopt policies and practices that promote healthy foods, and researchers should work with retailers to assess arrangements of retail space that would support healthy choices while maintaining profits.
- Until the system is fixed, shoppers should be wary of supermarket trickery. Supermarkets today are as much about selling shelves to food companies as they are about selling food to customers.



Placement of products at checkout induces impulse buys.



It is hard to see Clemmy's ice cream in this freezer case, because it is behind a giant placard promoting sales of Häagen-Dazs (owned by Nestlé).

Introduction

Clemmy's sugar-free ice cream was no one's idea of a health food. Like many ice creams, it was high in saturated fat, which promotes heart disease. But it was sugar-free and was a product that would not cause a dangerous spike in the blood sugar of people with diabetes. Clemmy's was also lactose-free and offered consumers a lower-calorie option than the super-premiums it sought to compete against. "Even with no need to purchase products with no added sugar I could actually see myself picking up this pint again," gushed the ice cream blog, *On Second Scoop*. More raves followed.

And yet at the end of 2015, Clemmy's went out of business. Its failure shows how today's food marketplace is tilted in favor of the world's largest food manufacturers and against everyone else—including companies offering better-for-you products.

Clemmy's was the brainchild of Jon Gordon, a Southern California entrepreneur. For years Gordon indulged a pint-a-day ice cream habit that abruptly ended in the summer of 2006, when his doctor ordered him to stop. He was at risk of developing type 2 diabetes. Gordon tried substituting sugar-free ice pops. He scoured the grocery store in search of other sugar-free frozen treats. Reading

the ingredients list, he worried about the artificial chemicals used. The products he tried were either flavorless or left, he said, “an unpleasant aftertaste.” At the end of 2006, Gordon bought a high-grade ice cream maker with the idea of making his own sugar-free ice cream.

Gordon was working in commercial real estate at the time. He had worked in advertising and marketing earlier in his career, and his resumé even included a stint as a movie producer. He didn’t know anything about making ice cream but he’d work until 2 or 3 AM in search of the right mix of flavors. Eventually he discovered xylitol, a sugar-free sweetener made from corncobs or hardwoods like birch.¹ By February 2007, he believed he had created a great-tasting vanilla ice cream. A quest that had started as a self-indulgence began to feel like a potential business. He launched Clemmy’s in 2007 with a five-product offering: vanilla, chocolate, coffee, toasted almond, and chocolate mint swirl. Only later did he realize that devising a sugar-free ice cream that people craved was the easy part.

Retail sales of ice cream are dominated by two food giants: Nestlé, which produces Häagen-Dazs, Dreyer’s, Edy’s, and Skinny Cow, and Unilever, which sells Ben & Jerry’s, Breyers, and Klondike, among other products. These days most big grocery chains also sell their own private-label ice cream. Gordon did the math on the real estate that makes up the frozen-food section. The average supermarket reserves maybe 24 freezer doors for frozen desserts. Twenty-two of them, Gordon calculated, were committed to Nestlé, Unilever, or a store’s own brand. “That left only about two doors for the rest of us,” Gordon said. The competition was fierce, he added, “meaning the stores could charge what they wanted to get space on one of those shelves.” Getting into most retail chains meant paying a fee: a “slotting” fee for every new flavor he wanted to introduce in each store he wanted his product.

Gordon would get lucky with Albertsons and the 350-odd stores it operated in southern California. Apparently, its buyer liked his product, and he received a reduced rate: a one-time fee of \$30,000

¹ Large amounts of xylitol may have a laxative effect, leading to diarrhea.

for three flavors. “That was nothing compared to what other stores were asking,” Gordon said. But he also got only what he paid for—distribution, he said, only in some of Alberstons stores.

Gordon tried to get into Stop & Shop, which is owned by Ahold, a Netherlands-based grocery store giant. They asked, he said, for \$110,000 per stock keeping unit (SKU)—in this case, a one-time charge for each flavor of ice cream he sold in the chain’s 400 or so stores. That would have meant writing a check for more than half-a-million dollars to sell all five of his products in this one chain. He passed. Safeway didn’t require that he pay slotting fees at all (except, then it only carried Clemmy’s in a small fraction of its stores), but most chains wanted something like \$20,000 to \$40,000 per SKU. He’d write a check for \$50,000 to ShopRite, but again he’d be disappointed: even a check that size, he learned, didn’t secure him freezer space inside all of the chain’s stores.

“I’m getting my product out there, but it’s costing me,” Gordon said. He created another three flavors but that only meant paying more fees. So too, did his introduction of ice cream bars and a product called Ice Cream O’s (imagine the ice cream equivalent of a donut hole). By the end of 2012, Clemmy’s was being sold in roughly 9,000 stores. Gordon estimated that he paid more than \$1 million in slotting fees yet he was still only selling some of his product in a fraction of the country’s 38,000 grocery stores (FMI, 2015). “You don’t start a food company thinking you have to deal with payola, but that’s what it was all about,” he said.

The payments didn’t end there. Success had its own price, as the food broker Gordon had hired to help him negotiate with the chains explained. Some chains charged a different kind of placement fee sometimes called “pay-to-stay”—a kind of annual rent to retain a spot inside the freezer cabinet. Sometimes these meant cash payments, but often compensation took the form of “trade”—cases of product Gordon would have to send at no cost to the store. Pay-to-stay fees are typically not as great as the slotting fees a manufacturer must pay to get inside the store, but they added up. Some chains demanded that Clemmy’s provide two or three cases of free ice cream per store per year to remain on a

shelf. That worked out to between \$40,000 and \$60,000 a year for a retailer with 1,000 stores.

Then there were the dollars retailers extracted through quarterly promotions, like the “buy one, get one free” sales that retailers would run on his ice cream. All of it was spelled out in what insiders call a Cooperative Marketing Agreement—a six-month or one-year deal that delineates how a retailer and manufacturer share marketing costs. “I’d get the bill from the store and laugh,” Gordon said. “They’re contributing ten cents to the cost [of the sale] and I’m contributing 50 or 75 cents.” These agreements typically required him to periodically offer deep discounts on his product through manufacturer coupons, which meant tens of thousands of dollars in additional costs and razor-thin profit margins that barely covered his overhead.

“If you complained, you were told, ‘If you want to play with the big boys, this is what you have to do,’” Gordon said.

But the big boys, Gordon learned, had advantages beyond their advertising budgets and the deep pockets that let them buy as much freezer space as they wanted. There was also the clout conferred on them by the stores as so-called category captains. The stores use what’s called a planogram to dictate where precisely products go on their shelves. Incredibly, stores commonly rely on the category captain—Hellman’s (owned by Unilever) in mayonnaise, Quaker Oats (owned by PepsiCo) around hot cereals—to draw up the planogram for its stretch of shelving. Nestlé was the category captain for frozen desserts in 22 of the country’s 25 largest supermarket chains, Gordon said, while Unilever likely served as captain in the other three. “I wanted six flavors, but they’d recommend that the chain only to carry two or three,” Gordon said. They’d relegate him to a lower shelf in a less desirable corner of the freezer case, far from their products—“behind a hinge...so that you can barely see it,” as Gordon told the *Desert Sun* in Palm Springs in 2013 (Perrault, 2013). Sales were steadily increasing each year. Consumers seemed to like his product. But he felt frustrated by a system he saw as favoring entrenched giants over smaller challengers.



This Frito-Lay schematic instructs its delivery crews to use multiple displays, including freestanding "gondola" shelving units, tiered shelves called "risers" that go on top of the gondolas, and gondola "snack center" displays that go on shelving units called "relay" racks. It also includes checkout displays called "FEMs" (front-end merchandisers), including a type of checkout display called a "mini max," and planograms for checkout to "rock the register." "C foods" refers to convenience foods, such as Munchies crackers and Grandma's cookies, both of which are also made by Frito-Lay. Frito-Lay instructs its delivery personnel to display snack foods on aisles along the perimeter of the store.

Gordon was hardly alone in his resentments. A few years after starting Clemmy's, Gordon was named to an advisory board of the Grocery Manufacturers Association, chosen, he believes, "to represent the interests of the small and medium-sized businesses." GMA is the nation's largest association of food manufacturers. Executives from other, modest-sized food makers would pull him aside at meetings. They had their own complaints about placement fees and a category-captain system that allowed their strongest competitor to determine where their products appeared on a shelf.

Clemmy's and Gordon filed suit against Nestlé in 2013, accusing the food giant of anti-competitive practices. The final straw had been a deal Gordon thought he had with Kroger, the country's largest supermarket chain. Kroger was on the verge of taking Clemmy's national through its 2,400 stores, Gordon alleged in his lawsuit, until Nestlé intervened. "Unfair, monopolistic business practices in the food industry harm not only competition," the suit alleged. "[T]hey also decrease the diversity of nutritional options available to consumers, causing public health to suffer as well."

In its suit, Clemmy's laid bare the close, symbiotic relationship between the large food manufacturers and their counterparts inside the big grocery chains, which were racking up big profits selling their sodas and candy bars and bags of snack food. "Large food manufacturers such as Nestlé possess disproportionate access to and control over supermarket decisions," the company alleged in its complaint. Clemmy's shared its marketing strategy and promotional schedule with one grocery chain—and, through legal discovery, learned that that plan had ended up in the hands of a Nestlé brand manager.

"We want a fair playing field not only for Clemmy's but for other small companies like us," Gordon told a local reporter in 2013. "Secondly, the big losers here are consumers. If small companies can't innovate and get new products on the shelf, what's the incentive for entrepreneurs in this country?" (The Public Record, 2013). Nestlé denied any wrong-doing—and described the lawsuit as a "transparent ploy to manufacture publicity for a brand that may be struggling because it has failed to win with consumers or for other reasons that have absolutely nothing to do with Nestlé" (Progressive Grocer, 2013).

"...the big losers here are consumers. If small companies can't innovate and get new products on the shelf, what's the incentive for entrepreneurs in this country?"

No jury would ever hear the case of Clemmy's v. Nestlé. A California Superior Court judge dismissed the case in May 2015, a few weeks before it was to go to trial. Gordon had lost, and now his company was an industry pariah. Where once Clemmy's was selling in 9,300 stores, fewer than 400 stores were carrying his product by the fall 2015. "The retribution was enormous," Gordon said. By year's end, he felt forced to declare Chapter 7 bankruptcy.

"Between slotting fees and the category-captain system, those two things alone make it almost impossible for a smaller manufacturer to make it," Gordon said.

Why It Matters

A Tilted Playing Field

Plenty of healthy products have become fixtures of today's supermarket. Dole, Fresh Express, and Earthbound Farm Organic brands have bagged, dark-green, leafy salads, such as baby kale. Fat-free Chobani and Fage Greek yogurts are staples in dairy cases around the country. Kashi cereals, Sabra hummus, Pepperidge Farm whole-grain breads, Barilla whole-grain pastas, Blue Diamond almonds, and Silk soymilk: are all found in supermarkets.

Yet how many smaller companies (some with better-for-you products) are thwarted at least in part because the big supermarket chains generally charge fees that only the largest manufacturers can pay?

In 1999, the U.S. Senate Committee on Small Business & Entrepreneurship held a hearing on slotting fees. Those few industry insiders willing to testify hid themselves behind a screen and spoke through a voice-altering apparatus. "Nothing but a device to exploit money from manufacturers and squeeze all the independent and smaller processors off the shelves and out of business," the chairman of a small Ohio-based food manufacturer told the committee. Another small food maker made the claim, "I know for a fact that my competition is paying the lease on the buyer's BMW" (Jennings, 2015).

Moved by such testimony, Senator Christopher Bond, the Republican chair of the Small Business Committee, instructed the U.S. Government Accountability Office (the agency that provides auditing, evaluation, and investigative services to Congress) to investigate. Despite a promise of confidentiality, not a single person from inside the supermarket industry stepped forward. “I have worked for the GAO for 31 years and this is the first time I have had to report to committee that I have been unsuccessful in trying to carry out the work,” the GAO’s Lawrence Dyckman testified when submitting his report a year later (Copple, 2002). The Senate committee’s next step was to ask the Federal Trade Commission (FTC) to study slotting fees and other placement fees.

In 2001, the FTC released a 79-page study titled the “Report on the Federal Trade Commission Workshop on Slotting Allowances and Other Marketing Practices in the Grocery Industry” (FTC, 2001). Its conclusion? Further study was needed before policy makers could even discuss this tectonic shift inside the grocery store business. (“If retailers and manufacturers were willing to be candid in a public fashion with us,” one FTC official said at the time, “this report could have been more conclusive” (Wilkie, 2002).)

With concerns being voiced about anticompetitive concerns, the FTC secured an additional \$900,000 in federal funding. The goal, the agency reported, was “completion of its investigation into slotting fees in order to ensure fair competition in the retail grocery business” (FTC, 2003). This time the agency would take a much narrower focus. Its investigators would look exclusively at slotting fees (charges to get a new product into a store) and limit their inquiry to five product categories (hot dogs, bread, salad dressing, ice cream, and pasta). The FTC noted that slotting fees shut out smaller competitors and meant fewer choices for consumers. But the 65-page report the FTC released in 2003 came to the same conclusion as the first: further study was needed before the agency could take action.

The FTC was in Republican hands then, as was the U.S. Department of Justice. Some law professors argued that fees extracted by food retailers amounted to commercial bribery. Others raised antitrust concerns. But a pair of economists argued precisely

the opposite in a 2006 paper posted on the DOJ's website. They perceived a "procompetitive business justification for contractual arrangements that involve the manufacturer purchase of retail distribution" (Klein, 2006).

In sharp contrast, New York University nutrition and food studies professor Marion Nestle wrote in her book *What to Eat* about the payments that retailers charge a food manufacturer for placement: "This unsavory system puts retail food stores in firm control of the marketplace. They make the decisions about which products to sell and, therefore, which products you buy. This system goes beyond a simple matter of supply and demand. The stores create demand by putting some products where you cannot miss them. This is why entire aisles of prime supermarket real estate are devoted to soft drinks, salty snacks, and sweetened breakfast cereals, and why you can always find candy next to cash registers (Nestle, 2006)."

For years, public health advocates have been calling for a better understanding of the impact of placement fees on the design of the typical grocery store, which influences consumer choices. Of particular concern has been the cost of placement in high-traffic zones at the ends of the aisles and by checkout counters, where shoppers are induced to purchase impulse items. A deeper understanding of supermarket real-estate pricing has never been more important than today, when people are in need of healthier options.

"Study after study has shown us that it matters where food is placed and matters a lot," said Mary Story, a leading scholar in the field of child and adolescent nutrition and child obesity prevention and Associate Director for Academic Programs at the Duke Global Health Institute. But not nearly as well understood are the economics of that relationship. "If you look at the checkout aisle and the endcaps, it tends to be soda and snacks and other highly processed foods," Dr. Story said. "If you want people to eat healthier—and if you don't want them to get soft drinks or Pop-Tarts or chips or any of these foods that are highly processed—we need to better understand the factors that put those foods there in the first place."

Location, Location, Location

Outside of the meat, produce, and dairy sections, nearly every inch of today's store is for sale. That means that the layout of a store is more about what manufacturers want than the desires of consumers.

"You're talking about a deep, dark secret of the retail world," Mark Heckman said when asked about placement fees. Heckman, a former marketing executive with Marsh Supermarkets, a chain operating 75 stores in the Midwest, is now a partner at Accelerated Merchandising, a research company specializing in grocery store

economics. "Retailers don't want this information getting out there. They don't want one brand to know what the other one is paying."

"People have the reasonable assumption that a product is where it is on the shelf for reasons other than a manufacturer paid a lot of money to put it there."

– Gregory T. Gundlach, a marketing professor at the University of North Florida

Placement fees vary greatly region to region and from chain to chain. Prices depend on any number of factors, including the number of stores in a chain and the food category in which a company is competing. Sometimes a retailer has set prices, depending on where in a store a food

manufacturer needs to be, but more typically, manufacturers say, negotiations feel like "Let's Make a Deal." The food manufacturer that agrees to increase its promotional spend with a retailer or reduce the price it charges the store for its product can in turn reduce a slotting or a pay-to-stay fee. Some retailers are known for charging higher prices (supposedly stores on either coast charge more than those in the middle of the country). Certain chains always charge slotting fees, while others might give a break to a smaller manufacturer, or at least one with a hot new product they think customers crave.

To glimpse into this opaque world, this report uses a strategy of triangulation: speak to enough people inside the industry to get a

good sense of the range of fees a food manufacturer would need to pay for everything from middle-of-the-store slotting fees to a premium spot near the register. Given the variations between prices paid to stores, between products, and between negotiated package deals, it is only possible to estimate approximate costs. “It’s difficult to find any hard numbers,” Heckman said. “And any numbers you find would be only relevant to that one category [in that one chain].” Smaller food makers generally proved happy to share numbers when asked—so long as they could do so anonymously. “I don’t need stores angry with me because I gave away their trade secrets,” one executive told us. Several brokers who help food manufacturers negotiate these deals also proved game even as they stressed that concrete numbers were hard to come by. But other brokers declined to share what they saw as proprietary information. “These are a private contractual matter between trading partners,” one said. “Why in the world would I share that?”

The most valuable real estate in the store is the checkout aisle, which one broker calls “the beachfront property” of the supermarket.

The most valuable real estate in the store is the checkout aisle. “This is the beachfront property,” said a broker who specializes in checkout economics, but preferred to remain anonymous. There, space is sold by the inch. One broker told us that the typical store is charging \$3 an inch for placement by the register for a

few months. Another said \$3 was on the low side. “The average chain is charging at least \$5 an inch,” he said. The higher number was confirmed by a third broker, who spoke about deals that have crossed his desk that have a manufacturer agreeing to pay a single chain more than \$500,000 to get its product by the registers of all its stores—with the hope that it would sell well enough to remain there for the duration of the 52-week deal and not just the few months the store was guaranteeing through the placement fee.

When asked about what it would cost to place a hypothetical Better-For-You bar by the register, these brokers stressed is that even if a manufacturer had the money, it wasn’t clear the stores



Placement at checkout comes at a premium. Brokers said that it could cost \$3 to \$5 per inch to get one candy bar in the checkout. It could cost upwards of \$5 million for one candy bar to secure a spot on a shelf at checkout in the 50 biggest supermarket chains for several months to a year.

would sell a spot there. “They have a lot more demand for space than they have space available,” one broker said. “And are they telling Snickers they need to move to make room for you or M&M’s?” So stiff is demand for space at the front of the store, he said, that “retailers can get away with charging pretty much what they want.”

Six inches of shelf space is what a Better-For-You bar would need for the “candy caddy” (basically a thin cardboard box) to hold the product. The typical supermarket has ten or twelve checkout lanes. Assuming \$3 an inch (and a dozen checkout aisles), that works out to just over \$200 a store. Five dollars an inch adds up to more than \$350 a store. Using those estimates, a few months in the checkout aisle for a Better-For-You-Bar would cost around a quarter million dollars in Safeway’s 900 stores. Triple the number to get inside Kroger’s 2,700 stores. (Numbers like this demonstrate just how impressive it is that discount supermarket chain Aldi committed to remove all candy from all checkout aisles in all its stores by the end

of 2016.) And, despite the high costs, stores would not guarantee that the Better-For-You bar would get more than a few months by checkout. To get one product of this size into the checkout displays of the 50 biggest chains—which collectively operate 22,000 stores—a food company would need to pay upwards of \$5 million for a few months, possibly a year.

Yet stores have no trouble selling this space because it's that valuable to manufacturers. Candy makers have to be there. That's because nearly two out of every three people entering a store don't visit the candy aisle (Goldschmidt, 2013). But everyone needs to go through checkout. Those six inches by the register, where impulse buying is high, can account for more than half of a candy maker's profits in a store, according to a food broker who specializes in securing companies a place by the cash register.

The economics are different for the soda and chip makers. Sales of the two-liter bottles of soda and family-sized bags of chips keep the factories working at peak efficiency. But it's the sale of smaller-sized snack versions that stores sell by the cash register that generate the lion's share of the profits. Coca-Cola—and the stores—make very little on the two-liter bottles and the 12-packs of cans that stores are constantly running on special. "No one is making money on that two-liter bottle," one broker said. "Not the bottler and not the retailer." But the individual 20-ounce plastic bottles people grab from a refrigerated box in the checkout line generate enormous profits. (That's why convenience stores devote so much space to refrigerated single-serving bottles.) Similarly, Frito-Lay makes a lot more profit on the small \$1.49 bags of Doritos people buy on impulse while waiting to pay for their groceries than the big bags advertised in the circular for \$3.49.

"If I'm Coke or Frito-Lay, I'm paying whatever I have to so as to get placement by the cash register," one broker said. "That placement is so valuable to their profitability model."

That property is equally valuable to the store and not just because of the extra cash placement fees bring in. Rare is the deal, the brokers tell us, where a store makes more on the placement fees than on sales of the product itself. It happens, the brokers say,

but when it does, that item will be booted back into the middle of the store. The country's supermarkets are able to get away with markups of 40 percent or more above wholesale on items they sell by the cash register. These items only account for about \$6 billion a year in sales—barely 1 percent of a store's overall sales—but generate industry-wide profits of \$2.4 billion a year—about one-fourth of the industry's overall profits—before factoring in placement fees.



Soda companies make more money from selling single-serve bottles at checkout than they do from the 2-liter bottles stocked in the soda aisle.

Retailers also charge steep fees to have a product featured on an “endcap” (end-of-aisle display) or other displays around the store. The prices for those premium spots tend to make them off-limits to all but the largest manufacturers. Even getting a product inside the store will stretch the budgets of many food companies. “If you want your product inside a store, you’re going to have to pay,” one food broker counseled.

The small subset of food manufacturers that can afford the prime retail real estate—checkout and endcaps—shape the look and feel of the supermarket. The assortment of products available, and which ones are showcased in key areas known to prompt

“If you want your product
inside a store, you’re going to
have to pay...”

impulse buys, isn’t determined by consumer demand, or even by what has sold well in the past. Instead, back-room deals between corporate titans

influence the selection of products most visible and accessible to customers, ultimately driving sales of the particular products that end up in our grocery carts. “I often hear about companies that have a real hard time getting into the major supermarkets because the big players have basically locked up the shelf,” said Jennifer Harris, director of marketing initiatives at the Rudd Center for Food Policy & Obesity at the University of Connecticut. That in itself wouldn’t be a health concern—except that nutrition analyses demonstrate, Harris said, that newer, smaller food makers generally offer “healthier products with whole grains and less sugar, sodium, and fat” than larger manufacturers.

“It’s sad,” said an executive who has worked both for large and smaller-sized food makers. “The country is demanding healthier products, but you can’t get into some of these grocers without scale. It doesn’t make a difference how good a product is for you or how much people might like it. If you don’t have the money, you can’t play the game. You’re buried in the back of the store—if you can get inside at all.”

Still, some public health experts look at the big food manufacturers and see progress. The Nestlé’s and Unilevers of the world, says Tracy Fox at Food, Nutrition & Policy Consultants, are introducing new, better-for-you products and reformulating existing ones so they are healthier. But like others in the public health field, Fox stressed that it’s often the smaller companies that tend to be promoting better eating. It’s the story of every industry, where smaller, nimbler players are better able to innovate than larger companies—and in food, many innovations these days support healthier eating.

One pressing question, according to Fox, is “how smaller manufacturers break into the grocery store with its ‘pay to play’ mentality.”

When defending themselves against criticism over slotting and other placement fees, industry insiders sometimes point to KIND Snacks. KIND, which has sold more than 1 billion of its nut- and fruit-based bars over the past decade, has clearly made it. It has done so remaining an independent company. But Daniel Lubetzky, the company’s founder and CEO, feels fortunate he started when he did. “When I was starting in 1993, slotting fees were just starting to become more prevalent,” Lubetzky said. But then a kind of merger mania took over the grocery industry in the mid- to late-1990s, Lubetzky said, “leaving stores with a lot of debt. So they started charging, charging, charging for everything and slotting ended up becoming more common and more institutionalized.

“It’s harder now than it was in the early days when I was getting started,” Lubetzky said.



Food companies pay to introduce new products and to stay on supermarket shelves.

DEFINITIONS

“Cooperative advertising”—typically, cost-sharing between retailers and food manufacturers for locally placed advertising, such as weekly circulars or Sunday newspaper inserts, but in some cases, manufacturers may pay up to the full cost of advertising.

“Placement fees”—the fees a food manufacturer pays for placement of its product anywhere in a store, whether by the register, on an endcap (an end-of-aisle display), by the deli, or on a shelf.

Synonym: “Shelving fees”

There are three kinds of placement fees:

“Display fees”—payments for premium spots like an endcap, cardboard displays that retailers call “shippers,” or the “shelf talker” signs on shelf facings that call attention to a product.

“Pay-to-stay fees”—payments food manufacturers must make to remain on a store’s shelves. These are not necessarily cash payments; often manufacturers compensate retailers in the form of free merchandise and reduced prices.

Synonym: “Staying fees”

“Slotting fees”—the fees manufacturers pay to introduce a new product on a store’s shelves. Some people use “slotting fee” more generically to refer to any payment a manufacturer makes for space inside a store. But in this report, the terms “slotting fees” and “slotting allowance” are used to describe payments made for new products.

“Trade promotion”—describes a wide range of payments that manufacturers make to retailers. That includes placement fees and also payments for special seasonal promotions, two-for-one sales that manufacturers pay for, and the hefty charges manufacturers pay to be included in circulars and newspaper inserts. These are typically spelled out in a Cooperative Marketing Agreement signed by both the manufacturer and retailer.

Synonyms: “Promotional allowances” and “trade spend”

In 2008, there was excitement among proponents of better eating when Bolthouse Farms hired Jeffrey Dunn as President and CEO. Dunn, who had spent twenty years inside Coca-Cola and became president of Coca-Cola North America and Latin America, vowed to “make carrots cool” using the marketing techniques he learned at his old employer. He and the other big-food executives he had recruited to Bolthouse would do the same for its line of vegetable-based juices, protein drinks, smoothies, and yogurt-based salad dressings. Seven years later, Bolthouse Farms was bought by Campbell Soup Company for \$1.55 billion. “You can beat your head against the wall trying to get some traction inside the store or you play the game,” one insider there told us. Operating inside Campbell, the insider said, “we have the money and the might to make sure our product gets out there.”

How We Got Here

A Land of Giants

Today’s grocery store landscape is dominated by giants, starting with Walmart. Walmart—the country’s largest retailer—sells more groceries than any other company in the country. The behemoth makes about one-fourth of all grocery sales in the United States (\$298 billion in total sales in 2016, of which 56 percent, or \$167 billion, were grocery sales). The country’s largest supermarket chain is Kroger, with reported sales of \$110 billion in 2016, of which \$83 billion were grocery items (including food, floral, and health and beauty). Kroger alone accounted for 10 percent of the country’s supermarket sales in 2015.

Albertsons is owned by AB Acquisitions, which also includes Jewel-Osco, Shaw’s, and Star Market. At the start of 2015, AB Acquisitions bought Safeway (Safeway, Vons) for more than \$9 billion. In the summer of 2016, the Federal Trade Commission allowed for Royal Ahold (Stop ‘n Shop and Giant Food) to merge with Delhaize, a European-based company that operates Food Lion, Hannaford, and Sweetbay in the United States. Also in the top-five is Publix, which booked \$32.4 billion in sales in 2015. Together, Walmart, Kroger, AB Acquisitions, Royal Ahold/Delhaize, and Publix account for nearly half the groceries sold in the United States.

LARGEST RETAILERS BY MARKET SHARE

Rank	Company	Fiscal Year-end Sales (000)	No. of Supermarkets	Top Banners
1	Wal-Mart Stores Inc. Bentonville, Ark.	\$298,378,000*	4,132	Walmart Supercenter (3,465) Walmart Neighborhood Market (639)
2	The Kroger Co. Cincinnati	\$109,800,000	2,623	Kroger (1,143) Harris Teeter (232) Ralphs (137)
3	AB Acquisition LLC Boise, Idaho	\$58,322,940	2,290	Safeway (894) Albertsons Store (285) Vons (204)
4	Publix Super Markets Inc. Lakeland, Fla.	\$32,400,000	1,114	Publix (1,105) Publix Sabor (6) Publix GreenWise (3)
5	Ahold USA Inc. Quincy, Mass.	\$26,400,000	788	Stop & Shop (423) Giant Food/Carlisle (196) Giant Food/Landover (169)
6	H-E-B Grocery Co. San Antonio	\$23,000,000	315	H-E-B (261) H-E-B Plus (36) H-E-B Central Market (9)
7	Delhaize America Inc. Salisbury, N.C.	\$18,058,000	1,283	Food Lion (1,096) Hannaford (187)
8	Meijer Inc. Grand Rapids, Mich.	\$16,700,000	223	Meijer (223)
9	Wakefern Food Corp. Keasbey, N.J.	\$15,700,000	187	ShopRite (120) Price Rite (62) The Fresh Grocer (5)
10	Whole Foods Market Austin, Texas	\$15,389,000	419	Whole Foods (419)

Progressive Grocer, 2016

The remaining top-30 retailers, including Wakefern Food (ShopRite, PriceRite), Whole Foods, Target, and Trader Joe's, together operate 7,300 stores and book \$198 billion in sales annually. The country's remaining independent supermarkets each logged under \$3 billion in sales in 2015—accounting for less than 5 percent of the country's supermarket sales that year.

A Shift in Power

“When I first got involved in the industry, the manufacturer had more power than the retailers.” That’s according to Hank Cardello, who starting in the 1980s worked in marketing or brand management for a series of large food manufacturers, including General Mills, Nabisco, and Coca-Cola. Today he is a senior fellow and director of the Obesity Solutions Initiative at the Hudson Institute. “But over time that has literally flip-flopped,” Cardello said. “These days manufacturers are kind of at the mercy of the retailer. They have to do whatever the retailers say.”

“Brands have resigned themselves to the fact that retailers are the power brokers in their relationship,” said supermarket expert Mark Heckman. The same small universe of retailers, he said, see the same presentations from the same small group of big food companies—Coca-Cola (Sprite, Powerade, Honest Tea), PepsiCo (Gatorade, Tropicana, Quaker Oats, Frito-Lay), Mars (M&M’s, Snickers, Twix, Milky Way, Wrigley, Uncle Ben’s), Mondelēz (Oreo, Chips Ahoy!, Triscuit, Cadbury, Nabisco), and a few others. “They know all the [food] manufacturers are fighting for that same exact space, letting the stores charge more,” Heckman said. “To get to the consumer, they have signed on begrudgingly to putting more into the buckets of money brands designate to pay retailers.”

Ultimately, the consumer pays. Whenever a food company secures premium placement in the supermarket by making a payment to a supermarket or providing a discount on merchandise or free product (“free fill”), preferential placement drives sales and one way or another the cost is passed along to the consumer. Companies either work harder to get consumers to buy more of their products or build the fee into the price.

Putting Big Food’s Interests First

It was A&P—more formally, the Great Atlantic & Pacific Tea Company—that first started charging food companies for retail marketing, according to Herb Sorensen, a supermarket consultant with more than 35 years in the business. Starting around the 1920s, A&P started printing up a weekly flyer and charged brands that

wanted to be featured within its pages. “This is pivotal,” Sorensen declared. “This is the beginning of retailers charging the suppliers for access to their customers.”

The Journal of Law and Commerce, Journal of Marketing, and Marion Nestle are among those declaring that slotting fees began in the 1980s (Jennings, 2001; Bloom, 2000; Nestle, 2006). But it seems likely that another East Coast chain, ShopRite, created the slotting fee in the 1970s. Bruce Weitz, then a young buyer for ShopRite, was often the one who had to break the news to any food manufacturer wanting space on his company’s shelves. The rationale: it took a lot of work to introduce a new item into its product mix, starting with a new slot in its warehouse. And it cost again to swap out a product proving a dud. Why not charge food manufacturers a “slotting fee” for the trouble? Early on, Weitz said, the going rate tended to be three cases of free product per store.

“We got whiff a few years after we started that A&P was copying us,” Weitz said. Other local chains picked up the idea and from there the idea spread. By 2000, Nielsen data showed that 85 percent of retailers were charging slotting fees (Wilkie, 2002).

But why stop at a charge for new items? “You’ve got all these manufacturers wanting access to their customers,” Sorensen said. “So what do they do? They start charging a fee just to be on a shelf. They start charging more for premium placement.” Consultants like Sorensen urged the stores he worked with to capture any revenue they could from manufacturers. The typical supermarket had 10 or 12 checkout aisles and 20 endcaps. Keep prices low, he advised, and make your money on placement fees and promotions. The result is an upside down world in which manufacturers are paying retailers.

“Make no mistake, the supplier is the store’s real customers,” Sorensen said. “[The suppliers] need a store’s customers—and they’re willing to pay for access to the traffic a good store attracts.”

Food manufacturers pay these fees, in other words, because they have no choice. The stores are the gatekeepers—and these central players in the grocery ecosystem need to be part of any discussion about improving America’s diet. Deborah A. Cohen, M.D., a senior

natural scientist at the RAND Corporation and author of *A Big Fat Crisis: The Hidden Forces Behind the Obesity Epidemic—And How We Can End It*, said: “Where things are in a store influences what people purchase.”

Lock Up a Space

Manufacturers initially opposed slotting fees as a kind of tax on new products.

“Slotting seemed nothing more than a rip-off of vendors by retailers—yet another scheme to make money on the buy rather than on the sell,” wrote Warren Thayer, editorial director of *Frozen & Refrigerated Buyer*, in a 2015 column to accompany a long feature his magazine published about slotting fees (Thayer, 2015a). One trade publication (he left it unnamed) ran an outraged editorial every month, according to Thayer, vowing to continue until slotting fees were abolished. That magazine would go out of business but the slotting fee would remain.

Over time, the food industry’s biggest players learned to embrace placement fees and the advantages it gave them in their competition with smaller foes. “We loved them,” said a former top marketing executive at Coca-Cola when asked about placement fees. “Absolutely loved them because it lets you lock up a space.” Indeed, over time, manufacturers have shifted their spending from what he and others call the “air wars”—advertising—to the “ground wars” of battling it out inside the supermarket. “It is generally well-known that in many industries, money has increasingly shifted out of advertising budgets over time to build up trade promotion budgets and in-store marketing,” Gregory Gundlach, the University of North Florida marketing professor, wrote in the mid-2000s (Gundlach, 2005). In 1968, manufacturers spent an estimated 28 percent of their overall marketing budgets on trade promotion; most of the rest was spent on advertising. By

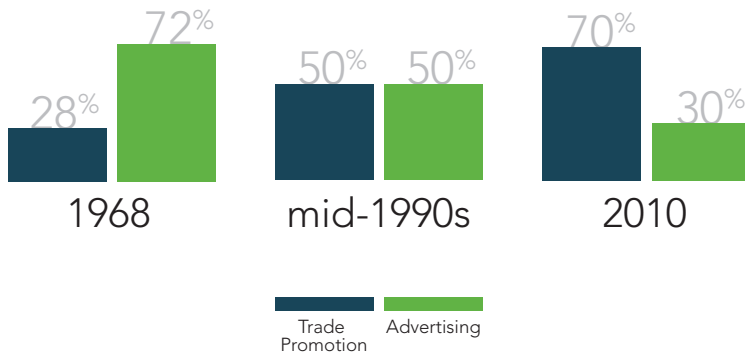
“Make no mistake, the supplier is the store’s real customers,” Sorensen said. “[The suppliers] need a store’s customers—and they’re willing to pay for access to the traffic a good store attracts.”

the mid-1990s, manufacturers were spending around the same amount on the “air” and “ground” wars. The ad budgets of the big food manufacturers would continue to rise but promotional spend increased at a much faster clip. By 2010, according to the American Antitrust Institute, manufacturers were spending more like 30 percent on advertising and the rest on trade spend—using the layout of the supermarket to push their products on consumers (American Antitrust Institute, 2013).

The trouble with that shift, according to Gundlach, is that many people think that products are displayed in particular parts of the

store because of consumer demand, not realizing that the manufacturer paid a lot of money to get them there.

MARKETING BUDGETS OF FOOD MANUFACTURERS



American Antitrust Institute, 2013

To the big manufacturers, trade spend has become “a built-in cost of doing business,” according to an ex-Coke marketing maven, echoing what others said. Trade fees typically comprise 15 to 20 percent

to a manufacturer’s costs—the second largest expense for many food manufacturers, behind only the cost of creating the product itself. So for every \$1 billion Coke or Pepsi spends on producing, distributing, and advertising its drink, it spends about \$150 million to \$200 million in placement fees and other expenses to give its brand a leg up inside the supermarket.

How Food Manufacturers' Payments Affect the Consumer Experience

The Two Million Dollar Entry Fee

Slotting fees have come a long way since ShopRite's demand that manufacturers pay them a kind of new-product tax of three boxes per store. Even a small grocery chain these days charges around \$8,000 or \$9,000 to introduce a single new product into the freezer case of all its stores, the trade magazine *Frozen & Refrigerated Buyer* reported in 2015 (Thayer, 2015b). That number "can leap quickly to \$20,000 or even into the range of \$100,000 [for a single item] at some major chains," the magazine found. The price is a lot higher than that, of course, if a product comes in several flavors.

The "all-in price," according to *Frozen & Refrigerated Buyer's* survey of industry prices? The "national rollout of a single frozen SKU," the magazine concluded, "can run to \$1.5 million to \$1.6 million" (Thayer, 2015b).² Others have reported an all-in price of up to \$3 million for select food categories in large supermarket chains.

Those figures are in keeping with other, more formal surveys of placement fees. According to a 2001 study published by the *Journal of Law and Commerce*, Frito-Lay paid an average of around \$100,000 per chain (more for larger chains and less for smaller ones) to introduce a new product, while Truzzolino Pizza Roll paid \$25,000 to Safeway to get on its shelves chain-wide. Apple & Eve spent somewhere around \$150,000 just to get its "Fruit Punch Product" into a limited number of stores around the Northeast, leading the study's authors to conclude that slotting fees "are not a mechanism for new product introduction but rather a means for thwarting it" (Jennings, 2001). The 2003 FTC survey of five product categories estimated that the national rollout of a new product (to get into 80 to 90 percent of supermarkets) would cost between \$1 million and \$2 million, depending on the product (FTC, 2003).

The freezer case is typically more expensive than a shelf in the middle of the store. One broker said he warns clients that it could cost as much as \$66,000 per SKU to get into all of Kroger's 2,300

² *Frozen & Refrigerated Buyer* added the necessary caveats whenever talking about placement fees. Prices vary dramatically and spending more on promotions can often lower the slotting fees a manufacturer pays.



stores—unless they want a spot in its freezers, in which case it would cost a lot more than that. But not every section of a store has a price tag, he said. Stores seldom assess slotting fees in the produce section. A 2006 paper written by a pair of economists notes that slotting fees are rare in the milk case and also in the meats and seafood aisles (Klein, 2006). But as a result, that’s where produce, milk, seafood, and meats stay in the supermarket—in their designated cases, and not in multiple locations in the store that repeatedly remind and prompt people to buy soda, chips, and other foods.

A spot in the soda aisle will cost a company—a lot. Mark Heckman of Accelerated Merchandising estimates that a company with a new cola could expect to pay \$2 million in slotting fees for a national rollout. Yet Heckman, who for years worked as an executive at Marsh Supermarkets, doesn’t see that payment as out of line. “If the product is successful, that \$2 million will be peanuts,” he said. “It’s a one-time shot. Over the life of a product, that \$2 million won’t even register.” However, that does not figure in the annual promotional fees that the manufacturer would pay to keep the product on the shelves.

Plus, that assumes a company could afford to pay \$2 million to cover slotting fees while also ramping up its production facilities and spending money getting the word out about its new product. The head of sales at a medium-sized manufacturer specializing in organic products recalls the company's early days as a small player trying to gain a foothold inside mainstream stores. Slotting fees were "a big hurdle early on," she said. Often, she said, they chose to sell their products in the health and beauty aids section, where the fees were much lower. Still, even those less expensive deals typically ate up the first six to nine months of profits. These days the company can afford better placement inside the store but it also comes at a steep price: its product comes in a variety of flavors and the pricier chains are charging her company \$20,000 per SKU. At times she has been able to negotiate lower slotting fees, but invariably that has meant upping the "trade spend" and committing to paying for other store programs.

One insider said his company typically pays between \$5,000 and \$20,000 per SKU, depending on the size of the chain, to get a single variety of its condiment on the shelf. Some chains have demanded free product in lieu of a cash payment but "we're paying one way or another," the insider said. "It's not negotiable: if you want to be in his store, you're writing a check or you're giving them a free fill per store per SKU." And the cost of entry will be higher for products vying for a place in the dairy case. "They're going to expect a heftier price because space there is more limited," he said.

Hampton Creek, a plant-based food company known for vegan mayo, will introduce as many as 30 new SKUs in 2016, according to the company's director of retail, Jordan Tetrick. That could add up to millions in slotting fees. But Hampton Creek doesn't resent paying them, Tetrick said, "because they're a one-time payment and we want to be in there for the next 50 years. You need to be on that shelf, so you pay." It helps that Hampton Creek has the financial backing of several billionaires, including Microsoft co-founder Bill Gates, Yahoo co-founder Jerry Yang, and Li Ka-shing, who Forbes magazine has described as Asia's richest man. The company has raised nearly \$30 million in venture capital since its founding in 2011.

For those without that kind of financial backing, however, slotting fees can prove a large burden. As far back as 2001, the FTC reported that several manufacturers said “they had refrained from introducing new products because of the cost of slotting allowances” (FTC, 2001). Think, too, of the large food company

“There are [a] million different factors that go into every deal,” one long-time food broker told us. “But the bottom line is you’re generally paying for shelf space.”

thinking of introducing a healthier version of a product. In that scenario, slotting fees add to the risk of introducing a healthier new product—the food company would need to pay \$1.5 million or \$2 million in slotting fees on the new version of its product.

Pay-to-stay placement fees are not as widespread as slotting fees. Several of the smaller food makers that were interviewed for this

report said that while retailers pressured them to spend money on endcaps, shippers, and to participate in other promotional programs, they weren’t required to pay any charges beyond the initial slotting fees. Yet pay-to-stay fees are routine in certain other parts of the store, including checkout and apparently the freezer case. Clemmy’s, for instance, was required to give free fills—two or three cases of ice cream per store per year for every SKU—to keep its spot in the freezer cabinet. At some of the bigger chains, that worked out to around \$50,000 a year, Jon Gordon said—a hefty annual property tax that proved a large burden to a modest-sized business like his.

There is cause for optimism. Stores are feeling pressure from customers and health advocates alike to sell a healthier mix of foods—and in at least a few cases that has translated into a reduction in fees. The organic-food sales executive quoted earlier said that 2015 proved to be a pivotal year for her medium-sized company. Placement of its products at checkout and other premium spots had largely been off limits in many chains but she has sensed a shift inside the industry. She’s starting to see better-for-you foods in checkout lanes. “Retailers are coming to us saying they want

healthier products by the check stand," she said. "If you have a product that helps them reach their goal of providing a healthier product mix, we're finding everything is negotiable."

The good news, she continued: "Once you're in, you're in, so long as your product is turning and you're meeting expectations." The bad news: "Sometimes we can't get a seat at the table to even start talking about healthier products."

Added KIND Bars' Daniel Lubetzky: "A lot of retailers who normally have little else but candy at checkout realize it's not good for business." That has translated into invitations to KIND to put its bars by the register. "We're starting to see the conversion of a lot of these checkout aisles," Lubetzky said. "And they're not asking us to pay any money."

WALMART

For years, Walmart, the country's top grocer, rarely charged slotting fees. Instead, the retailer demanded lower prices from its suppliers.

But that changed in mid-2015, when the company announced that it would start charging a fee to stock new items in its stores. A Walmart spokesperson told the Reuters news service, that the change was motivated by the fact that they were imposing a slotting fee on select suppliers but not everyone. But Kurt Jetta, the founder of TABS analytics, a retail analytics firm, said the new policy is the result of pressures to pay its workers a better wage and other bottom-line considerations.

"It's not the way Walmart has done business in the past," Jetta told Reuters. "This approach suggests that they are seeking areas to offset their increased investment in wages, as well as offset their lack of organic revenue growth" (Layne, 2015).

Yet Lubetzky also sees placement fees as a huge impediment to companies smaller than his own. He's an investor in several startups selling better-for-you products; invariably, he finds himself counseling patience. "What you do is start super-super slow," he said. "You start in specialty food stores. They don't charge slotting, they just want the product. Then you go to the natural stores. Some are charging slotting now but if your product is really, really exciting and [you] have a strong sense of mission, maybe they'll be more flexible." Then with some momentum behind the product—and cash in the bank—they'll be able to negotiate decent slotting fees. "The disadvantage of doing it this way," Lubetzky said, "is it takes a very, very long time to get your product out there."

Endcaps, Shippers, and Pedestals

Everything seems for sale inside the supermarket. There's the space in an extra wide aisle to place palettes of a drink maker's product; there, soda makers pay for their turn to sell their product at near cost, to help build brand loyalty, and to keep factories humming. There are the "shelf talkers"—also called "shelf signs"—that provide a way for stores to make extra money for products displayed on shelves in the middle aisles. The area around the deli counter is another hot property that stores sell to manufacturers looking for another place in the store to tempt customers with soda and chips. In recent years, there's even been talk of "mid-caps"—an extra-large shipper that protrudes from the shelf midway down an aisle. Not quite as profitable as their more desirable first cousins, the endcap, these special displays in a middle of any aisle have given double-digit sales boosts to those buying the space.

"Every retailer has this long menu of things they charge for," one food broker said. "They've got this program and that program they want to sell you. They've got 'front-end programs' and 'advantage programs.' A lot of the talk is about displays and endcaps and how much more of your product they can sell if only you'll commit to spending all this extra money."

Endcaps are typically the second-most-expensive real estate inside a store (after checkout). They're "the powerhouses of any store,"

grocery store consultant Sorensen wrote in 2009 (Sorenson, 2009). Research shows that the ends of aisles are one place where items are more likely to be bought on impulse. These are often used for seasonal promotions that pepper the year, from New Year's through Super Bowl and Valentine's Day, to Memorial Day, to the Fourth of July, Back to School, Halloween, Thanksgiving, and Christmas. Shippers and other cardboard displays are similarly expensive. Every new food manufacturer wants its products to have their turn on display but the question is who can afford this special treatment. One broker told us about a deal he had just negotiated on behalf of a small food manufacturer. It was with a modest-sized chain of around 300 stores. He described it as a "limited duration, one-time event" that would last a few weeks. Yet the retailer was still charging \$17,000.

This same broker brought up Publix, a chain of around 1,100 stores in the southeast and, to his view, one of the premier players in the grocery industry. "Publix'll push for six to eight high-visibility promotional programs a year," he said. Each "event" costs



Companies pay for end-of-aisle ("endcap") displays to help ensure that shoppers see—and buy—their products.

roughly \$75,000 at Publix and though the store often ties together multiple products and companies (chips and soda around Super Bowl), the price adds up. “I’ve seen where the price of entry is a minimum of \$175,000,” he said—commit to at least \$175,000 worth of promotional programs for the year or your product will never have its turn in the spotlight. “You’ll get the support of Publix—the space, the ad support, the whole nine yards,” he said. “But they’re incredibly expensive.” (If \$60-odd per store doesn’t sound like much, consider how much it would cost to have a single event inside of all 38,015 of America’s supermarkets: \$2.2 million.)

Then there’s the other promotional costs invariably associated with an end-cap promotion. That will roughly double the price of entry, said one former executive at a large grocery store chain. “At my store, if you said you wanted an end cap for two weeks, I’d say, ‘Great, but you also have to put the product on sale because otherwise it won’t be an efficient use of real estate.’ You’re doing buy-one, get-one-free or 30 percent off,” which he said increase the cost of a single event by as much as \$50,000 to \$100,000 per chain.

“You should sit in on one of these negotiations,” said one food broker. “You would think the stores were selling [to] the manufacturers rather than the other way around.”

Trade Spend

“Trade spend” is the catchall term that industry insiders use to describe the range of payments—in dollars and in kind—that manufacturers make to grocery store chains to promote their products. It includes placement fees (including slotting fees and pay-to-stay fees), placement in endcaps, and other displays,

price promotions and coupons, and in-store signage. There’s a charge to be included in a store’s weekly circular and, trade spend can also include the fee a retailer charges to have a product featured on its website. “Vendor allowances” and “promotional spend” are other terms used to describe the range of payments manufacturers make to stores to push their products. And then stores often demand that their suppliers provide free cases of products.

“Retailers don’t like talking about slotting or placement fees,” explained Accelerated Marketing’s Mark Heckman. “It sounds a bit down and dirty. So they talk about promotional fees or trade spend.”

An April 2016 report from the investment bank Barclays concluded that the typical food manufacturer devotes roughly 20 percent of its sales revenues to trade spend (Lazar, 2016). “Placement fees are only a part of the equation,” says a former executive for a larger grocery store chain. This executive encouraged anyone concerned about the hurdles in the way of smaller, more innovative food makers to look at the overall trade spend as part of the real estate costs associated with getting inside a store.

“If you don’t do some kind of sampling, if you don’t do buy-one-get-one-free or 20 percent off, your product won’t move fast enough and it’s taken off the shelf,” this former grocery store executive said. “The full picture of how difficult it is for these companies to get into a store has to take into account the full trade spend.”

He added, “Why do you think there’s so little innovation in the food space? These are the hurdles that make it very hard for smaller companies to get into the store and then stay on the shelf.”

How much are these fees worth to grocery store chains? Safeway provides an example. The California-based grocery giant is now privately owned,³ but when it operated as a publicly traded company, it revealed the worth of its “vendor allowance” deals in the paperwork it filed with the Securities and Exchange Commission. The store defined vendor allowances as slotting fees, promotional payments from manufacturers, and what it dubbed “contract allowances.” Contract allowances are what this report calls placement fees, minus any slotting fees. As Safeway defined it, “Under a typical contract allowance, a vendor pays Safeway to keep product on the shelf for a minimum period of time or when volume thresholds are achieved” (US SEC, 2015).

³ Safeway and Albertsons merged in 2015. The company is now owned by an investment group led by Cerberus Capital Management, a giant of the private equity world.

Safeway collected \$2.5 billion in vendor allowances in 2014. Slotting fees for new product introductions, the company said in paperwork filed with the SEC, made up only a “very small portion of total allowances,” but that’s not to say other placement fees weren’t critical to Safeway’s bottom line. Safeway wrote, “Promotional allowances make up the vast majority of all allowances,” and that included the selling of “a preferred location in the store.” The store collected \$2.4 billion in vendor allowances in 2013, and \$2.3 billion in 2012 (US SEC, 2015).

Placement fees and other promotional dollars have proved critical to Safeway’s bottom line. The company showed gross profits of \$9.7 billion in 2014 and \$9.2 billion in 2013, meaning that \$2.5 billion in payments is significant to its business model. (Safeway’s annual sales in those years were \$36.3 billion (2014) and \$36.1 billion (2013).)

The Bottom Line on Fees

Safeway’s transparency made it an outlier among supermarket chains. “Retailers were generally never happy to disseminate the information we were seeking,” said Gundlach, the Florida marketing professor.

Still, there are ways to estimate the size of this market. Working with other academics, Gundlach and his colleagues in the mid-2000s used what he called “leakage”—tidbits included in the footnotes of public filings and stray data points found in trade publications—to estimate the amount of money manufacturers pay retailers each year. Using “back of the envelope calculations,” Gundlach said, he and his colleagues figured that trade spend by food manufacturers large and small added up to \$50 billion a year.

Yet those dollar figures pale when compared to the calculations of a five-person research team inside Goldman Sachs. Together consumer product goods companies (including food, beverage, tobacco, and household products) pay stores more than \$200 billion a year in trade fees, according to a report the investment bank released in November 2015 that declared trade spend a “vital source of income for retailers” (Goldman Sachs, 2015).

Herb Sorensen, the supermarket consultant, said that the way the industry works now, the fees manufacturers pay stores—what he calls “supplier profits” or “backroom profits”—mean everything to a retailer’s bottom line. “That’s the number-one source of profits for stores,” Sorensen said.

“Within an Arm’s Reach of Desire”

Inside Coke, they called it “360 degree marketing.” That approach to store placement was the embodiment of a long-standing goal inside the company that Coke should be “within an arm’s reach of desire” wherever you are in the world. The ex-Coke marketing executive explained 360 degree marketing this way: “We wanted to have Coke next to the deli sandwiches. We wanted Coke in a cooler at checkout, we wanted an endcap, we wanted a vending machine. We wanted to have 10 or 20 places at a single grocery store.”

Coca-Cola has put its products within an arm’s reach in many grocery stores. If people skip the soda aisle, they still may be reminded and prompted to buy soda at endcaps, freestanding displays, and checkout. By contrast, there are rarely additional opportunities or prompts to purchase fruits or vegetables outside of the produce section.

PepsiCo of course has the same goal as Coke. Its competitive edge is in its ownership not only of sugary drinks, but also of brands such as Frito-Lay. “In the U.S., about 50 percent of the time, when people buy a salty snack they also buy a refreshment beverage,” PepsiCo explained in its annual report in 2011, “so we can capitalize on the leading positions of our iconic brands in both categories to drive the purchase of our snacks and beverages together. As we grow globally, this idea is more powerful than ever” (Pepsico, Inc., 2011).

If people skip the soda aisle, they still may be reminded and prompted to buy soda at endcaps, freestanding displays, and checkout. By contrast, there are rarely additional opportunities or prompts to purchase fruits or vegetables outside of the produce section.



Even if customers avoid the soda aisle, “360 degree marketing” strategies ensure they will be prompted to buy soda several other places in the store.

Pepsi dubbed this approach the “Power of One.” One broker described it as a “scale strategy to block out other players.” Its representative, this broker said, “goes to a Kroger or a Safeway or any of the other big chains and says, ‘We’re Frito-Lay, we’re Mountain Dew, we’re Quaker Oats, we’re Gatorade. If you agree to all these placements and pairings and all this trade spend we’ll commit to—if you agree to the entire bundle—we’ll give you a kicker price, we’ll give you a premium.’” In other words, Pepsi will pay extra so that its Fritos or Lay’s chips are paired with Pepsi or Mountain Dew on an endcap or freestanding display. “Under those arrangements, Coke will be in a store but Pepsi will have more prominence,” said one broker. Of course, Nestlé, Mondelēz, and the other food giants have their own bundles of products and their own salespeople looking to hammer out deals with the grocery chains.

“I’ve seen grown men cry over what a competitor did [to] them in [an] aisle,” said supermarket consultant Sorensen. “A store doesn’t care if you’re company A or company B. They’re going to go with the most favorable deal term. There’s only so many square feet on that shelf. There are always winners and losers in that battle.” In fiscal year 2015, the Campbell Soup Company cut back its promotional spend on ready-to-serve soup—and for that and other reasons, saw its sales in that category fall by more than 5 percent over the following months.

FIGHTING BACK—AND LOSING

Frito-Lay grabbed the attention of industry insiders when it challenged the notion that it needed to pay so much money for placement inside the stores operated by one of the world’s largest grocery chains.

“This was like five years ago,” one broker told us. “They said, ‘We’re not going to pay placement fees and dared the retailer to drop their product.’ The retailer said, ‘Fine, we’ll give you a space in the chip aisle but nowhere else in the store.’” Frito-Lay is Fritos and Lays potato chips, of course, but also Doritos, Cheetos, Tostitos, Ruffles, Sun Chips, and Cracker Jack. “Frito-Lay was saying, ‘You don’t understand, we’re Frito-Lay.’ But the retailer was saying, ‘No, you don’t understand, I’m the retailer and I’m the gateway to your customer.’” It was Frito-Lay that backed down.

“When you negotiate with the big chains, it’s clear who holds most of the cards,” another broker said. “The real estate is too important to the biggest brands and the stores know that.”

The ex-Coke marketing maven is more specific about who is usually on the losing end of these negotiations. “If you’re this little organic guy or healthier guy,” he said, “trying to get a healthier bar or a healthier beverage on the shelf or checkout aisle, it can seem insurmountable because of the strength and scale of these players.”

The System and the Little Guy

For the smaller player, placement fees and other promotional payments present a significant challenge to starting a new business. (In fact, the fees represent so huge a hurdle that it's a non-starter for fruit and vegetable growers; few, if any, pay to get placement outside of the produce section.) "Slotting is a brick wall to small manufacturers, effectively blocking access to markets," a food manufacturer told *Frozen & Refrigerated Buyer* for its 2015 article about slotting fees. This vendor didn't doubt that the larger conglomerates liked slotting fees because "it can keep the smaller manufacturers'—often family-owned businesses—superior products off the shelf. I think that slotting also reduces consumer choice" (Thayer, 2015b).

Consumers never have the chance to try new brands that don't have the financial wherewithal of the big brands. Likewise, the only place they see fruits and vegetables is the produce section, meaning that even the most convenient and easy-to-eat fruits and vegetables never fully compete against packaged snack foods for a place in Americans' stomachs between meals.

The system is a self-enforcing feedback loop—companies pay for placement, placement sells their products, the companies spend some of the profits on placement, which sells their products, and on and on. While placement fees are not intended to discriminate against healthier products, it's difficult for customers, growers, start-ups, or health advocates to disrupt the cycle.

Supermarkets sell space in their advertising circulars alongside promotions for produce and meat. But even those smaller makers willing to pay for the privilege aren't necessarily welcome. When Jon Gordon of Clemmy's asked what it would cost to have his ice cream featured in the ads a chain runs in the Sunday newspaper, his contact told him, "Circulars are reserved for national branders. This guy says to me, 'Look, when you do the kind of business of a Nestlé and Unilever, then we'll talk,'" Gordon said.

"There are a thousand ways the system isn't fair to someone trying to do something innovative," Gordon said.

The category captain system seems one of the more overt ways the system is biased in favor of the largest food manufacturers. “There’s no consumer awareness of this,” according to Mumin Kurtulus, a professor of operations at Vanderbilt University’s Owen Graduate School of Management. “But the practice has proliferated throughout the grocery and consumer products industries and now has begun making inroads into apparel retailing as well.”

Under the typical arrangement, says Kurtulus, “the retailer shares all relevant information, such as sales data, pricing, turnover and shelf placement of the brands with the category captain” (Horick, 2012). The category captain is responsible for drawing up the planograms and also underwrites the costs of the data-mining and other analytics its designers ostensibly use to justify their decisions. (Whoever does the stocking—whether a representative of the food company or a supermarket employee—must follow the planogram, with the practice enforced by the category captains.) This gives the largest brands great influence over whether a rival’s product sits at eye-level or requires a consumer to bend or stretch up to reach it.

For stores, the category captain system is a way to save money and also keep its best suppliers—the world’s biggest food manufacturers—happy. But others have questioned the arrangement, including Thomas Leary, a Republican appointee to the FTC who served between 1999 and 2005. “As an antitrust matter, it seems rather strange that you’d have one company advising a store on how to handle the product of its competitors,” Leary told *Forbes* magazine in 2002 (Copple, 2002).

Leary would get no argument from many within the food industry. One large player in the organics food industry called it “a ridiculous, unfair practice that should be abolished”—and hers is a company that sometimes serves as captain in its small corner of the grocery store. “There’s a general feeling out there that some companies are paying for the privilege of being category captain and then use that advantage to tip the scales in their favor,” she said. Hampton Creek’s Jordan Tetrick shrugged off slotting fees as the cost of doing business. But selling an egg-free mayonnaise



Just Mayo pays for its place on the shelf, but a category captain like Hellman's (owned by Unilever) may decide which shelf it sits on.

means it's largely up to Hellman's (made by Unilever), the category leader, whether his products sit on a low or high shelf or at eye-level.

Other Retail Stores

Placement Fees and Convenience Stores

Grocery stores, of course, are not the only place people buy food. The United States is home to more than 150,000 convenience stores, according to the National Association of Convenience Stores. That grouping, which includes gas stations, mini-marts, and bodegas, racks up tens of billions in food sales each year. There, too, placement fees often play an oversized role in the food choices stores—and therefore its customers—make.

One study found that convenience stores (and also drug stores) in Louisiana devoted an average of 50 times more shelf space to soda, salty junk food, cookies, snack cakes, and candy than to fresh, canned, or frozen fruits and vegetables. In California, soda and junk food took up 20 to 30 times as much shelf space as produce (Farley, 2009). Another study found that less than one in 10 convenience stores in or around Atlanta sold whole-grain breads and that only 3 percent sold fresh vegetables (Glanz, 2007).

The convenience-store industry can be divided into two. There are the “corporates” and there are the “independents.” Large chains such as 7-Eleven and Circle K are a hybrid: many of their stores are corporate-owned, but others are owned by independent franchisees. It’s the corporates, which account for around 40 percent of the country’s convenience marts, that sell real estate inside their stores.

“7-Eleven gives its independents [franchisees] a lot of flexibility and so they put product wherever they want to,” said Joel Goldstein, the president of Mr. Checkout Distributors, a firm that specializes in placing new products inside convenience stores. “As opposed to a corporate-owned 7-Eleven, which goes strictly by a planogram.” WaWa, an East Coast chain, Goldstein said, “is very much a corporate store. Every WaWa strictly follows the planogram. There’s always going to be 5-hour Energy in the same slot. It’s always going to be the Tic-Tacs in the same place.”

There is good news to report from the world of convenience stores. 7-Eleven now sells seven times more bananas than its best-selling candy bar. Aiming to provide its customers a healthier offering of food, Love’s convenience stores, an Oklahoma-based chain with more than 350 locations across 40 states, sells fresh fruit at the checkout counter. And Kwik-Trip has committed to increase healthy options near its cash registers as well. Few if any of these placements involve slotting or placement fees.

Yet those are the exceptions. For the most part, food manufacturers are buying their way inside the convenience-store market. The fees manufacturers pay for prominent placement inside a corporate-owned convenience store, Goldstein said, are similar to those for

the supermarket chains. He quotes rates of between 25 cents to \$1.50 per store per SKU to buy a prominent place by the register for a week. The deals he negotiates typically involve hundreds of stores at once, if not in the thousands. "That translates into the millions of dollars," Goldstein said.

One of the chains Goldstein negotiates with is Dollar General, a discount operator that caters to a lower-income clientele. Dollar General, with more than 12,000 stores in 43 states, is "very much a placement-fee organization," Goldstein said. To make his point, he tells of a client who makes an energy drink. They offered to pay \$11,000 a week for a spot in the checkout aisle inside all the Dollar General stores, "but 5-Hour outbid us." On one hand, that works out to less than \$1 per store per week. On the other, Goldstein said, his client didn't think it could rationalize spending \$50,000 or more a month just to have its product prominently placed inside a single chain that would reach only a tiny fraction of potential customers.

Food Sales inside Non-Food Stores

The big grocery store chains may have invented the idea of charging for real estate inside their stores, but it didn't stop there. "[O]ther industries have begun to adopt similar practices," the *Journal of Law and Commerce* reported in 2001 (Jennings, 2001). Placement fees spread from the frozen-food section of supermarkets to a wide range of retailers, including those selling footwear, computer software, and auto parts.

Eventually, the big food manufacturers recognized that non-food retailers could serve as additional channels for selling their brands. These days it is common for stores selling everything from home goods to office supplies to give prominent placement to junk food and soda. Bed Bath & Beyond, for instance, often sells movie-theater-sized boxes of candy at checkout. Office Depot sells variety packs put together by Nabisco (including Oreo Minis and Nutter Butter Bites) and Frito-Lay (Doritos and Cheetos). The office-supply behemoth with more than 2,000 stores also pads its bottom line by selling soda, candy, and other snacks in its checkout lanes. Even hardware stores and toy stores are getting into food, pushing candy bars and other junk foods on their customers at checkout.

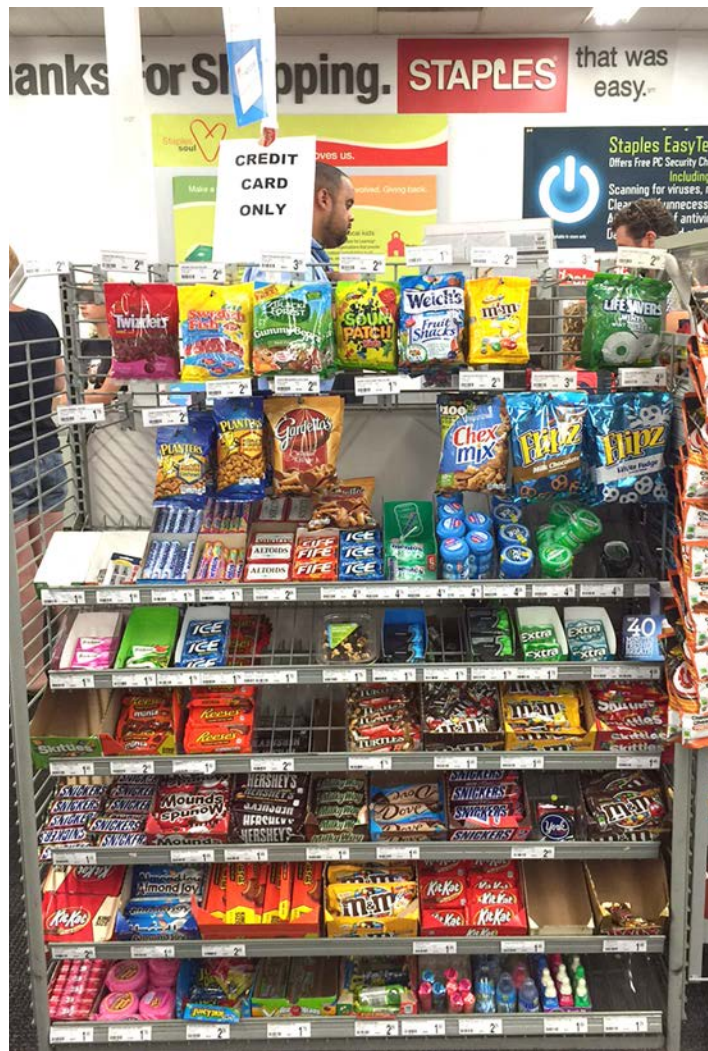
“These other retail channels have learned a lot from supermarkets,” explains Mark Heckman of Accelerated Marketing. “So they’ve made the effort to get into a limited number of food categories like chips, candy, carbonated soft drinks.” Even do-it-yourself stores like Michaels Craft Stores, Jo-Ann Fabric, and Home Depot are getting into the business.

“Any time you’ve got a captive audience,” Heckman said, “a retailer is going to see an opportunity to put items there that have the potential for an impulse buy.”

Non-food stores don’t typically charge a placement fee, informants say. Instead, the non-food chains demand a price break in exchange for prominent placement. “They’re happy to give you space in the checkout aisle,” a broker said. “But you have to be able to deliver profit for them to make it worth their while.”

Policy Recommendations

Most think of supermarkets as a nutritionally neutral space, where people have equal opportunity to purchase both healthy and unhealthy foods. What we see when we peek behind the curtain



Stores that are not even in the business of selling food—like Staples, an office supply store—now push candy at the checkout.

is that retailers and big food manufacturers make secret deals to push some products over others. Placement fees have a significant impact on the retail food environment. Stores feature particular products in the most prominent parts of the store—checkout, endcaps, and eye-level shelves and big food manufacturers drive which products are promoted through price promotions, signage, and other in-store promotions. The fees manufacturers pay retailers also influence the presence or absence of particular products and brands from store shelves altogether.

Placement fees matter because they determine the selection of products available to consumers and how they are presented to them, influencing which foods and beverages consumers buy and eat. The system is rigged against consumers, the produce industry,

“We have standards for so many things,” Dr. Deborah Cohen of the RAND Corporation said. “Car manufacturers are required to include seat belts and airbags. We need to figure out what the equivalent of a seatbelt or an airbag is in the design of a supermarket.”

and small businesses—against everyone except big food manufacturers and retailers. In light of this report’s findings:

- The Federal Trade Commission (FTC) should investigate the use of placement fees and other trade promotion practices (such as slotting fees and free products for in-store promotions and placement) in the retail grocery industry. The FTC should compel food retailers to provide information on their revenues from trade promotion practices and on related contractual arrangements with food and beverage manufacturers. Upon completion of the investigation, the FTC should issue a report detailing the extent of these practices, revenue generated, the nutritional quality of new products allowed on store shelves, and the potential impact the practices have on the competitive marketplace, including on public health, consumer choice, and food prices.
- The Securities and Exchange Commission (SEC) should determine whether disclosure of trade promotion practices should be required for publicly traded companies.

- State attorneys general should investigate whether the use of placement fees or the deference given to category captains violates antitrust or consumer protection laws and prosecute supermarkets whose practices illegally harm small businesses or consumers.
- Cities and counties should adopt healthy-checkout ordinances to ensure that the prime real estate of checkout is not used to undermine customers' diets and health.
- Retailers voluntarily should reserve a percentage of endcaps, checkout, and eye-level placements for healthful products that are moderate in saturated fat, salt, and sugars and contain whole grains, fruits, or vegetables. They should also assess whether the system of category captains poses a risk of prosecution for antitrust violations.
- Food and beverage manufacturers should do more to promote and place their better-for-you products—such as nuts, whole-grain breads and crackers, waters, and seltzers—on endcaps, at checkout, and in displays throughout the store, rather than aggressively promoting less-healthful products.
- Researchers should work with retailers to assess arrangements of retail space, pricing strategies, and promotions that would support healthy choices while maintaining profits.
- Shoppers should be aware of the tricks that companies use to get them to buy unhealthy products sold on endcaps and at checkout.

In short, supermarket shelves should not be for sale to the highest bidder to the detriment of consumers and small businesses.

Backroom deals should not drive Americans to purchase unhealthy foods in grocery stores. Given the high rates of obesity, diabetes, heart disease, and other diet-related health problems, the healthfulness of products should play a more prominent role in retail marketing. The supermarket industry claims to be in the business of “Feeding Families [&] Enriching Lives” (FMI, 2016). They could do more to put the interests of shoppers—their true customers—before those of big food manufacturers.

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