Fees and Services

All but five of the interviewed firms reported that fee and service requests from grocery retailers and mass merchandisers had increased; none reported a decrease. The five exceptions were California and Florida tomato shippers, who felt that requests were unchanged. Responses from the retailer interviews confirm the increase in fees and services. We asked shippers to describe their experiences with a list of possible fees and services. For each type of fee or service, we know if a shipper paid a fee or provided the service or had received a request to do so, but not to how many accounts it applied. Generally, firms reported that multiple buyers requested a particular type of fee or service.

Not all fees and services were necessarily viewed as harmful. Some were thought to enhance product movement or to provide competitive advantages to the shipper. In general, fees were viewed as more harmful than services, which likely explains the higher shipper compliance rate with services. Specifically, 17 percent of the types of fees requested were viewed as beneficial, 21 percent were viewed as neutral, and 62 percent were considered to be harmful. In contrast, 44 percent of the types of services requested were considered beneficial, 27 percent neutral, and 29 percent harmful.

Fees

On average, 3.7 different types of fees had been requested by retailers and mass merchandisers or offered by shippers in 1999 (table 12). As price takers, individual commodity shippers may not be able to pass fees along to buyers. As a result, with the exception of fresh-cut produce, shippers generally paid fees only when required to do so by their retail customers rather than using them proactively to capture greater market share from competitors.

Florida and California tomatoes had the least number of fee requests or offers (2.5 and 2.3) and grapefruit shippers the most, 5.4 (table 12). However, if the lettuce and bagged salad data are separated, bagged salad shippers experienced 5.8 types of fees. The relatively high incidence of fees for grapefruit shippers is puzzling. One explanation is that theirs is the only considered commodity with declining per capita consumption; retailers may request more fees to mitigate low grapefruit demand relative to supply.

Nearly half of all fee requests were reported to be new within the last 5 years. For lettuce/bagged salad shippers, however, fees appear more longstanding with only 30 percent reported to be new (table 12).

We asked how shippers dealt with requests for different fee types and the consequences of their actions. In the interviews, we provided four options for each type of fee request: the shipper complied with a request, did not comply but suffered no adverse consequences, did not comply and lost the account, or negotiated an alternative (see appendix). If a firm reported that they complied with a request for a particular type of fee, we do not know if they complied with a request for just one account or for more than one. For example, if all firms complied with a fee request for at least one

Table 12—Average number of fee types reported per shipper and dispositive of requests by product type, in 1999[1]

Item	Grapes	Oranges	Grapefruit	California tomatoes	Florida tomatoes	Lettuce/ bagged salads	All products
				Number per firm			
Average number of fee types requested by or offered to retailers and mass merchandisers[2]	3.2	4.3	5.4	2.3	2.5	4.7	3.7
				Percent of requests[3]			
Average share of new fee types among requested fee types[4]	52	59	49	61	47	30	48
Average share of requested fee types complied with	69	51	45	36	29	79	58
Average share of requests resulting in accounts lost when not complied with	33	47	47	15	100	63	41

[1] Results are based on a limited number of observations and must be interpreted with caution. The nine types of fees considered are listed in the box, "Fees."
[2] Shippers were asked if they paid a type of fee to any of their retail accounts. Thus, these results indicate the number of fee types paid to at least one retail account.
[3] Includes fees offered by shippers.
[4] New since 1994.

Source: Economic Research Service, Produce Marketing Study interviews, 1999-2000, USDA.

account, we would show 100 percent compliance but this does not mean that all firms complied with requests for 100 percent of their accounts.

Also, when firms have more than one account for any particular type of fee, they could report more than one option for dealing with requests. A firm with fee requests for more than one account could possibly report more than one outcome and perhaps all four; we do not have a one-to-one mapping of accounts and fee request disposition. As a result, the sum of the four responses does not necessarily equal 100 percent (although firms often reported the most common way they handled fee requests). For example, in table 12, for those grape firms receiving requests for the nine types of fees considered, 69 percent of requests were complied with for at least one account. Another 33 percent of requests had at least one account where the shipper did not comply with the fee and lost the account.

On average, shippers complied with 58 percent of the types of requests they received. Here, the differences among products were striking. Florida tomato shippers complied with only 29 percent of the types of fee requests they received, compared with 79 percent for lettuce/bagged salad shippers.

For 41 percent of the requests, shippers did not comply and lost business for at least one account. California tomato shippers appeared to suffer these consequences much less; only 15 percent of fee type requests not complied with resulted in lost accounts (table 12). In general, many California commodity firms indicated that although they didn't always lose an account when unwilling to comply with a special fee request, they often noted a decline in purchases from the firm in question. These firms expressed concern since they felt unable to fully measure the opportunity cost of noncompliance. In other words, it is difficult to know what would have happened with sales to an account if fees had been paid.

Volume incentives (see box, "Fees") are the most commonly provided type of fee with the highest cost to shippers. While some fees are new within the last 5 years, volume incentives have been used for years, although perhaps not at current levels. Volume incentives were requested of 73 percent of the firms interviewed, with only 18 percent of the requests reported as new (table 13).

Volume incentives are typically implemented as graduated incentives, with the discount per carton increasing when certain volume goals are met. When retailers respect these graduated volume scales, some shippers view their implementation as beneficial. In other cases, shippers report that retailers take the deeper discounts regardless of whether the volume goals are met. When billing and payment discrepancies of this type occur, some shippers are unwilling to engage in disputes for fear of losing a retail customer. More shippers consid-

Table 13—Fees requested by retailers and mass merchandisers, by type, 1999[1]

Fee type	Average share of firms: Providing fee[2]	Average share of firms: With a fee request[3]	Average share of requests[3]: New[4]	Average share of requests[3]: Complied with[5]	Average share of requests[3]: Lost account for noncompliance[5]
	Percent				
Volume incentives/discounts	40	73	18	68	33
Promotional allowances or cooperative advertisements	34	62	41	67	50
Other rebates	29	58	38	61	64
Free-product discounts	28	42	26	78	25
E-commerce fees	12	24	92	62	0
Buy-back unsold products or failure fees	11	22	42	58	25
Retail capital improvement fees	9	40	64	27	23
Pay-to-stay fees	8	27	93	33	63
Slotting fees	6	24	92	31	57

[1] Results are based on a limited number of observations and must be interpreted with caution.
[2] Shippers were asked if they provided a type of fee to any of their retail accounts. Thus, these results indicate the share of firms paying fees to at least one retail account.
[3] Includes fees requested, whether complied with or not, and fees offered by shippers to at least one account.
[4] New since 1994.
[5] For any fee type requested, a shipper may comply with a request, not comply and suffer no adverse consequences, not comply and lose an account, or negotiate an alternative. A shipper may have more than one account and more than one response for the same type of fee, so the four alternatives (even though we only report two) do not necessarily sum to 100 percent.

Source: Economic Research Service, Produce Marketing Study interviews, 1999-2000, USDA.

ered volume discounts as harmful or neutral rather than beneficial.

Still, volume incentives have the potential to promote more stable relationships between suppliers and retailers; as the retailer buys more units from the supplier, costs per unit decline, providing an incentive for the retailer to buy larger quantities (over the season) from a particular supplier. Shippers may also gain efficiencies in marketing by increasing the size of accounts.

Promotional fees or cooperative advertisements are the second most frequently requested fee, with 62 percent of shippers having either received requests or offered this fee (table 13). If there is a performance commitment on the part of the buyer to promote the product, shippers may gain—for example, if an advertisement for a product stimulates demand. However, many shippers question the return received from promotional allowances since it is often unclear to them how retailers are spending monies allocated to promotion and whether consumer demand is indeed enhanced. Demand for fresh produce is generally relatively inelastic within certain price ranges. Hence, within these ranges, lower prices may not stimulate greater product movement, discouraging retailers from reducing retail prices in accordance with f.o.b. price reductions. When this occurs, promotional allowances may provide a benefit to the retailers' bottom line without stimulating additional shipper sales.

Other rebates are simply a reduction in price with no benefit to shippers unless such a payment is critical to retaining an important buyer. Other rebates seem to have been present for a while as only 38 percent of the requests for other rebates were new. The compliance rate is relatively high at 61 percent, which may be related to the fact that 64 percent of the requests not complied with resulted in lost accounts—the highest level of any fee or service considered (table 13).

Twenty eight percent of shippers paid ***free-product discounts*** and they generally viewed this fee as reasonable. Shippers are used to this fee—only 26 percent reported that it was new in the last 5 years—and the compliance level was the highest of all the fees, 78 percent. Even for those that did not comply with this fee, just 25 percent lost accounts, a low rate for fees in general. These free product discounts are generally paid when retailers are opening new stores or warehouses.

E-commerce fees are charged by e-commerce firms to sell products using their electronic exchanges. These fees are new and only 24 percent of shippers had received a request, with 62 percent of requests complied with, and no one losing business by not complying. E-commerce fees may become significant if more

Fees

Volume incentives. With this type of fee, shippers and buyers agree that a per-unit rebate will be paid once a certain volume level is attained. Volume incentives are usually structured with graduated scales, increasing as certain target volumes are reached. This is a retroactive payment after sales for the season or a specified period are over.

Promotional allowances or cooperative advertisements. This is a fee that shippers pay to retailers to advertise their products. This may be a fixed, upfront fee or structured as a per carton allowance. There may or may not be a performance commitment associated with these fees.

Other rebates. This is a per-unit price reduction without any performance commitment, such as those associated with volume incentives.

Free product discounts. When a shipper offers a new product, a retailer may request a certain number of free boxes, usually a specific number per store. Conversely, when retailers open new stores, they may request free product from their suppliers.

E-commerce fees. Fees charged by new e-commerce firms to sell products using their electronic exchanges.

Buy-back unsold product or failure fees. Retailers may charge suppliers fixed fees when products fail or force shippers to take back product rejected at the distribution center level. A few shippers offer to buy back products that do not sell.

Capital improvement fees. Retailers request that shippers help pay for capital improvements, such as purchasing new refrigerated display equipment or new warehouse construction.

Pay-to-stay fees. These are upfront fees paid for an existing product to retain shelf space.

Slotting fees/listing fees/warehouse fees. Traditionally, slotting fees have been used to guarantee shelf space for new products. A slotting fee may be a one-time or an annual fee. Listing or warehouse fees are similar.

buyers incorporate e-commerce into their procurement systems. These fees were originally expected to amount to 1-2 percent of each invoice and many shippers indicate that their profit margins are insufficient to support this level of new expense. The e-commerce firms appear to be rapidly evolving toward fixed monthly fees as a more appropriate business model. Still, many shippers are concerned about paying any new fee to market to existing customers.

Although only 22 percent of firms reported a request for ***buy-back unsold product or failure fees***, they had a relatively high rate of compliance, 58 percent, largely due to a perceived lack of an alternative. Shippers may be asked to take product back upon arrival at a distribution center, even paying the return freight. While some requests are for product rejected as substandard, shippers also accuse retailers of rejecting product without Federal or State inspections in periods of abundant supply. This practice was viewed as very harmful to shippers, but few firms reported lost accounts due to noncompliance, largely due to the negotiation of alternatives such as invoice adjustments.

One of the fee types considered most onerous by shippers is a request by retailers for their suppliers to contribute to the cost of ***capital improvements***, such as the construction of distribution centers or refrigerated display equipment. Forty percent of the firms in our study reported having received this type of request, although the compliance rate was the lowest of the fees considered, likely because 100 percent of the requests were viewed as harmful. Some firms reported that even though they did not agree to comply, deductions were still made from their invoices for charges of this type. While at least three cases of requests to contribute to the construction of new distribution centers have been documented nationally, they appear to be relatively isolated occurrences compared with requests for sharing the cost of new equipment. However, requests to contribute to the cost of any type of capital improvement are included in these responses.

Fresh produce shippers are particularly concerned about ***pay-to-stay fees*** and ***slotting fees***. Slotting fees are fixed, upfront fees to retailers to guarantee shelf space for new products. Pay-to-stay fees are similar fees for existing products. Economists distinguish between these two types of fees (see box, "Economics of Slotting and Pay-to-Stay Fees"), but in practice they are often used interchangeably. We frequently consider the two fees together and call them slotting fees to simplify the discussion. Slotting fees first appeared in the nonproduce section of the grocery store beginning in 1984 (Sullivan, 1997) and have only recently become an issue for produce shippers. The emergence of slotting fees in fresh-cut produce has led to shipper concern that they will soon become standard for commodities as well.

A key finding of this study is that this does not appear to be the case, at least so far. Only two grape, three orange, three grapefruit, one California tomato, one Florida tomato, and three lettuce shippers reported that slotting fees had been requested for either a new or existing product. Requests were new within the last 5 years, except for one grapefruit firm. Shippers do not always distinguish between slotting fees and other fixed, upfront fees. In one case, a buyer required a shipper to pay a fixed, upfront promotional fee in order to gain their business and the shipper classified this as a slotting fee. One lettuce firm reported paying a slotting fee once, although it is not clear whether that was for lettuce or a fresh-cut product, but then decided not to pay again and lost the account. Several firms did lose accounts by not paying requested slotting fees—one of the orange shippers and all three of the lettuce firms. One grape shipper received a request for a $15,000 slotting fee, but successfully negotiated an alternative without losing the account. In the end, none of the commodity shippers interviewed were actually paying slotting fees.

Slotting fees are common for bagged salads and other fresh-cut branded products. Most lettuce/bagged salad shippers said that shippers initiated slotting fees in the mid-1990's in an effort to win new retail accounts and gain market share (see box, "Emergence of Slotting Fees in the Bagged Salad Industry"). A few bagged salad shippers said that retailers initiated slotting fees. When retailers were asked the same question, responses were mixed. About half said retailers had initiated slotting fees, while half said shippers had. Retailers agreed that slotting fees are used to obtain or increase shelf space. All bagged salad shippers received requests from retailers to pay slotting fees. Most paid slotting fees, either in response to retailer requests or to remain competitive with other shippers. Two firms did not comply; one was able to make an alternative arrangement, while the other, for whom bagged salads were a minor part of the business, lost the account.

Lettuce/Bagged Salads

Nearly all of the lettuce consumed in the United States is produced domestically. The vast majority of domestic production is situated in just two States: California and Arizona. Harvested area of head, leaf, and romaine lettuce in California and Arizona averaged 195,988, 41,538, and 29,213 acres, respectively, during 1992-99 and accounted for over 94 percent of U.S. acreage on average (USDA, NASS).

A relatively small number of shippers coordinate the growing, processing, and transport of lettuce. Nearly all the major shippers have headquarters and year-round sales offices in the Salinas, California, area. Domestic production throughout the year is facilitated by precise sequencing of production within and across major producing areas (Wilson et al., 1997). A typical sequence of production for iceberg lettuce begins in the Salinas Valley from April through October. Huron, California, briefly provides production while the industry shifts from Salinas to the desert areas of Yuma, Arizona, where production continues from November through March. Huron provides another brief production bridge between the desert and the Salinas Valley in March and April. Leaf lettuces may follow a slightly different sequence of growing regions, which could include the Santa Maria, Coachella, and Imperial valleys in California. Regardless of the geographic sequence, grower-shippers need to control the sequence of production to assure that no gaps occur in their year-round supply. Control can be achieved by many methods ranging from outright ownership, to handshake agreements, leasing, and contracts with various risk positions. While coordinating year-round production, harvesting, processing, and shipping across these domestic regions is a formidable task, it likely involves lower transaction costs than coordinating tomato shipments from Mexico or grape shipments from Chile.

Most shippers of iceberg, leaf, and romaine lettuce are diversified leafy-green vegetable shippers with large product lines including broccoli, cauliflower, celery, and many other products. Most of these Salinas-based shippers carry wide product lines as a way to offer their customers one-stop shopping. Some of these same shippers also focus on specialty items that have thinner markets. Several of the interviewed firms had expanded into the production and/or marketing of organic produce.

Many lettuce shippers engage in some degree of processing. Industry participants refer to processed products as fresh-cut or value-added items. Adding value may require relatively little processing, as is the case with leaf lettuces inserted into sleeves. Slightly more processing is required for items such as broccoli florets. But the level of investment and degree of sophisticated technology required for producing bagged salads is an order of magnitude greater than for other value-added products. Fresh-cut products like bagged salads require substantial capital investments in plants and machinery, in excess of $20 million for central or regional processing plants. The plastic films used in manufacturing bags must be designed for specific respiration rates of the processed vegetables inside the bag. Investment in research and development for new films continues constantly. Exacting logistics are followed to maintain the cold chain of the bagged products, because deviations from the ideal temperature could degrade product quality.

Commodities are undifferentiated products like unwrapped iceberg lettuce that may or may not be branded. These products have a price look-up (PLU) code but seldom have a universal product code (UPC) bar code. Value-added items like hearts of romaine are more likely to be branded, carry a UPC code, and are more convenient for final consumers than commodities. Fresh-cut items such as bagged salads may even include salad dressing and croutons. These items are usually branded, whether as a private label or that of a particular salad firm, and all salads are scanned at retail checkout.

Largely because of the barriers to entry in the bagged salad market, only five firms have effectively vied for major shares of the national retail market (table A). Competition for regional and national market shares has been intense, resulting in even larger market shares for the top two firms. From 1994 to 1999, the top two firms increased their joint market share from two-thirds to three-quarters of national mainstream supermarket sales. Some of the remaining three firms among the top five apparently shifted from branded products to private label. The number of competitors outside the top 5 firms shrank from 58 to 48 over the same period, while their joint market share also shrank from 6 to less than 3 percent of total dollar sales.

Table A—National market shares of fresh-cut salad sales in mainstream supermarkets

Firms/brands	1994	1999
	Percent	
Top two firms	66.1	75.5
Top five firms	91.2	87.6
Private-label brands	2.4	9.7
All other firms	6.4	2.7

Source: Information Resources, Inc.

Economics of Slotting and Pay-to-Stay Fees

Since slotting and pay-to-stay fees first appeared in the nonproduce section of the grocery store beginning in 1984, the economics literature on these fees is new and focuses on manufactured products and retailers.

Slotting Fees: In the narrowest definition, a slotting fee is a lump sum payment made by a supplier to a retailer for introducing a new product to the supermarket shelf. The standard set of assumptions used when analyzing slotting fees is that there is a limited supply of shelf space coupled with new product introductions. There is uncertainty about consumer acceptance of a new product, making the risk of new product failure unknown. Most researchers assume that manufacturers, as product innovators, have better information about product quality and consumer acceptance. Manufacturers may transmit information about product quality (or consumer acceptance of the new product) to retailers by offering to pay a slotting fee (Lariviere and Padmanabhan, 1997). Alternatively, retailers may request slotting fees from manufacturers, under the assumption that manufacturers of high-quality products (those that consumers are likely to accept) are more likely to pay slotting fees than are manufacturers of low-quality products (Chu, 1992). Some researchers argue that slotting fees might be the result of retailer market power, and can reduce consumer welfare by reducing output, increasing prices, or reducing product innovation (see the surveys by Bloom et al., 2000, and Richards and Patterson, 2000). Others argue that consumers benefit because slotting fees make it possible for new products to enter the market (Sullivan, 1997). The net benefit of the two (possibly) competing effects is difficult to predict, and would be specific to each particular situation. The overall welfare effect of slotting fees is largely an empirical question, which has not yet been addressed by researchers.

Pay-to-Stay Fees: Pay-to-stay fees are fixed payments manufacturers make to retailers for keeping their product on the shelf. Like slotting fees, pay-to-stay fees may result from retailer market power. Unlike slotting fees, pay-to-stay fees do not transmit quality information, since consumer acceptance of the product is already known. There are some alternative explanations for the pay-to-stay fee. First, retailing costs have been increasing, and the fee may be a way to allocate these costs between the supplier and retailer (Toto, 1990). An efficient allocation would spread the costs to the party that could most easily bear them; an efficient allocation is most likely when the parties have equal bargaining power. If one has a strategic advantage, however, the other might ultimately bear a greater cost (Gundlach, 2000). Second, the manufacturer might be paying the retailer to “not carry” a new, substitute product, another brand of a substitute product, or a private label product. Third, the fee might serve to place the product in a prime location, such as in an eye-level space on the shelf.

None of the bagged salad shippers would reveal the exact size of the slotting fees requested or paid by their firm, but several would talk about general use of slotting fees in the sector. For instance, shippers reported that slotting fees generally ranged from $10,000-$20,000 for small retail accounts to $500,000 for a division of a multiregional chain, and up to $2 million to acquire the entire business of a large multiregional chain.

Shippers typically negotiate annual contracts with buyers for fresh-cut products. The contract often contains a package of fees and services including slotting fees, volume incentives, and promotional fees. A contract is designed to guarantee a certain percentage of profit to the shipper regardless of the particular provisions, and some shippers argue that the distinctions between different fees and services have blurred. A few firms offer various contract proposals to their clients and allow each buyer to choose the preferred arrangement. Bagged salad shippers reported that the share of all fees ranged from 1 to 8 percent of sales.

Bagged salad firms were not clear what rights they obtained from paying fees. No firm mentioned slotting fees as a guarantee of a specified number of linear feet in refrigerated displays. A few mentioned using third-party or retailer scanner data to track sales. But it is not clear what happens when volume does not meet expectations. In a few cases, when one retail chain acquired another, previous slotting fee agreements were not honored.

Shippers selling private-label products, which are produced for a particular firm to sell as their house brand, do not pay slotting fees. Some bagged salad shippers have become much larger suppliers of private-label product as their branded market share has declined.

Emergence of Slotting Fees in the Bagged Salad Industry

The relationship between shippers and retailers has changed, but only part of this change is due to retail consolidation. Looking at the bagged salad industry and the emergence of slotting fees illustrates the complex interactions between several economic forces. In the early 1990's, three separate trends converged to produce the new bagged salad industry: the continuing interest of consumers for more convenient product forms, the evolution of new breathable films that preserve fresh-cut produce, and shippers' desire to add value to and differentiate their products. Unlike bulk fresh produce commodities such as lettuce or tomatoes, bagged salads are produced and marketed much like other manufactured grocery products, available every week of the year and requiring dedicated year-round shelf space.

Bagged salads achieved a rapid sales growth in the early and mid 1990's and new firms entered the industry. In 1994 and 1995, the growth in sales increased 49 and 32 percent over the previous year. Sales continued to grow in the late 1990's, although the rate of growth slowed to between 5 and 12 percent, and competition among shippers intensified. Slotting fees evolved in the mid-1990's within this highly competitive environment as part of a market share battle between competitors eager to protect their investment in costly salad processing plants.

Retailers typically sell two or three brands of bagged salads, with one being a private-label product. Many shippers want to capture the business of retailers. In addition to gaining a retailer's business, shippers also want to place specific products in stores. According to IRI data for mainstream supermarkets, the number of lettuce-based bagged salad items increased from 202 in 1993 to 464 in 1999. As the new industry launched many new bagged salad products, retailers were also coping with a large increase in products in the rest of the produce department.

Retailers have used slotting fees in the remainder of the grocery store since about 1984, even before the recent increase in retail consolidation. As the bagged salad industry developed characteristics of manufactured food products, it would not have been surprising for retailers to request slotting fees for bagged salads. However, most shippers reported that it was bagged salad shippers who first offered slotting fees as a means to garner market share from their competitors. The number of bagged salad shippers (selling to mainstream supermarkets) has declined from a high of 63 in 1995 to 54 in 1999. The percent of sales in private-label bagged salads, where no slotting fees are used, has increased from 2 percent in 1993 to 10 percent in 1999. Now fees are both offered by shippers and requested by retailers. Since retailers already asked for slotting fees for other products before the recent retail consolidation, these fees in bagged salads may not necessarily be a function of market power alone, but rather a combination of product characteristics, interfirm rivalry in a capital-intensive sector, and the relative negotiating strength between buyer and seller.

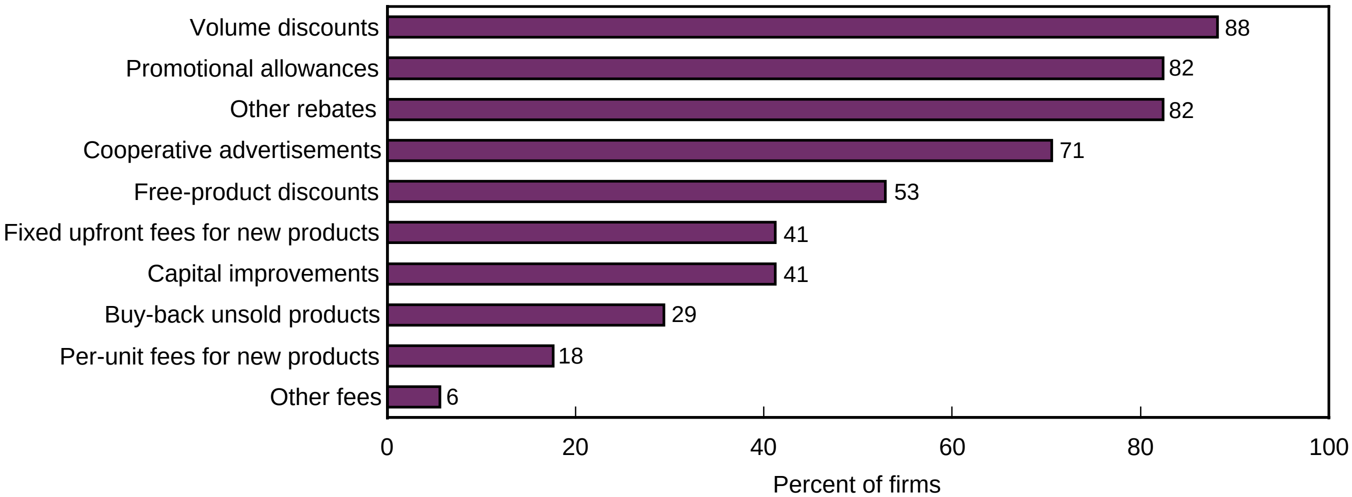
Slotting fees paid by shippers for their branded fresh-cut products may have a negative indirect effect on commodity shippers. A few bagged salad shippers also carry a broad product line of commodity products. Some shippers claimed that when such a firm negotiates a contract with retailers for its fresh-cut products, it might also negotiate terms favoring its commodity products. Thus, some commodity-only shippers could risk losing business. One firm redirected its marketing from retail due to retailers' tendency to purchase from suppliers that offer both commodities and fresh-cut products.

Retailers Report on Their Requests for Fees

Eight out of ten retailers agreed that the level of financial support provided by suppliers has increased. Retailers were asked about how fees vary across suppliers; they reported that fees are highest for their primary suppliers for each type of product, higher for fresh-cut and branded products, and lower for smaller shippers who have limited marketing budgets. As with shippers, retailers reported that the most common types of fees received from suppliers are volume discounts, advertising allowances, and other rebates (fig. 3). Eighty-eight percent of retailers said they receive volume discounts, while 82 percent received advertising allowances and other rebates.

Slightly more than half of the respondents used advertising/promotional allowances more often in 1999 than they did 5 years earlier. With the increased ability to measure sales by item, retailers can better weigh the costs and benefits of having an advertised sale on a product, balancing the lower price and the cost of the promotion with expected incremental sales and the allowance received from shippers. Seventy-one percent of retailers received fees for cooperative advertise-

Figure 3
Share of retailers receiving various types of fees in 1999



Source: Economic Research Service, Produce Marketing Study interviews, 1999-2000, USDA.

ments and 53 percent received free-product discounts. Fewer retailers (29 percent) reported that suppliers bought back unsold product. Over 40 percent of retailers said they receive fees from suppliers for capital improvements such as the purchase of refrigerated equipment or construction of a new warehouse.

As noted above, slotting fees and pay-to-stay fees are less common in the produce department than for branded grocery products in other departments. Seven of the 17 retailers/wholesalers interviewed (41 percent) said they received fixed upfront fees for new products, and another 18 percent said they received a per-unit fee for new products. The firms requesting fees were a mix of national and regional retailers and wholesalers. Some of the remaining 10 firms may have received slotting fees, but chose not to respond to this question.

Retailers reported that slotting fees were found primarily in branded categories such as bagged salads, baby carrots, and dried fruits and nuts. Retailers agreed that competition among bagged salad suppliers for market share is intense and that upfront fees are a way for shippers to obtain or increase shelf space. Hence, retailers concur that despite the current high profile of slotting fees in the produce trade press, they are not prevalent beyond the fresh-cut category, where they may be supplier as well as retailer induced.

Retailers use different business models. Not all retailers request slotting fees or accept them, even for branded, fresh-cut products. Some retailers focus on the efficiencies of handling relatively high-volume products, negotiating long-term agreements with suppliers, and then requiring these preferred suppliers to provide services such as automatic inventory replenishment, use of returnable containers, or other special packaging.

Services

Services requested by retailers, or offered by produce shippers, are on the rise. Retailers requested 4.1 types of services on average, slightly more than for fee requests (table 14). However, new service requests make up 77 percent of total requests, compared with 48 percent for fees. Several of these services, such as electronic data interchange (EDI) and category management, derive from relatively new information technology that provides both shipper and retailer with more timely market intelligence and means for information exchange, which could reduce costs and improve profits. However, some of these new technologies may impose substantive fixed costs, posing a competitive disadvantage to smaller shippers. Other new services such as third-party certification may be paid for on a per-unit basis, but also increase fixed costs by causing producers to change some of their operating systems in order to meet requirements.

Grapefruit shippers had the highest number of services requested or offered, with an average of 6.4 (table 14). Florida tomato shippers reported an average of only 2.7 services per firm, the lowest of the products considered. Across all products, 79 percent of the service requests were complied with, a much higher compliance rate than for fee requests. California and Florida tomato shippers were again the least likely to respond to the requests, lettuce/bagged salad shippers most likely. The high compliance rate for lettuce/bagged salad shippers has two components. First, some of the bagged salad firms offered services, such as EDI and category management, to their customers. Second, lettuce firms generally complied with the services requested by retailers, citing product quality and timely services as a way to trump competition and to cement ongoing relationships. Lettuce/bagged salad shippers reported no accounts lost due to not complying or offering a service, and orange shippers were most likely to lose business.

The most frequently requested service was ***third-party food safety certification*** (see box, "Services"), with 80 percent of the firms having received this request (table 15). In 1999 and early 2000 when the interviews were conducted, third-party food safety certification was just

Table 14—Average number of service types reported per shipper and disposition of requests, by product type, in 1999[1]

Item	Grapes	Oranges	Grapefruit	California tomatoes	Florida tomatoes	Lettuce/ bagged salads	All products
				Number per firm			
Average number of service types requested by or offered to retailers and mass merchandisers[2]	3.0	4.6	6.4	3.1	2.7	4.9	4.1
				Percent of requests[3]			
Average share of new service types among requested service types[4]	96	93	59	94	38	75	77
Average share of requested service types complied with	82	83	74	65	64	90	79
Average share of requests resulting in lost accounts when service not complied with	20	43	15	18	33	0	21

[1] Results are based on a limited number of observations and must be interpreted with caution. The eight types of services considered are listed in the box, "Services."
[2] Shippers were asked if they provided a type of service to any of their retail accounts. Thus, these results indicate the number of service types provided to at least one account.
[3] Includes services offered by shippers.
[4] New since 1994.
Source: Economic Research Service, Produce Marketing Study interviews, 1999-2000, USDA.

Table 15—Services requested by retailers and mass merchandisers, by type, 1999[1]

Service type	Average share of firms		Average share of requests		
	Providing service[2]	With a service request[3]	New[4]	Complied with[5]	Lost account for noncompliance[5]
			Percent		
Third-party food safety certification	47	80	72	71	0
Returnable containers/pallets	47	69	81	83	0
Special packs	45	65	80	83	33
Electronic data interchange or retail link program	34	56	90	73	25
Private labels	33	48	65	81	60
Automatic inventory replenishment program	25	35	90	84	33
Special merchandising displays	19	30	50	80	33
Category management services	19	28	80	80	0

[1] Results are based on a limited number of observations and must be interpreted with caution.
[2] Shippers were asked if they provided a type of service to any of their retail accounts. Thus, these results indicate the share of firms providing services to at least one retail account
[3] Includes services requested, whether complied with or not, and services offered by shippers to at least one account.
[4] New since 1994.
[5] For any fee type requested, a shipper may comply with a request, not comply and suffer no adverse consequences, not comply and lose an account, or negotiate an alternative,. A shipper may have more than one account and more than one response for the same type of fee, so the four alternatives (even though we only report two) do not necessarily sum to 100 percent.

Source: Economic Research Service, Produce Marketing Study interviews, 1999-2000, USDA.

Services

Provide third-party food safety certification. Suppliers are increasingly being asked to hire independent third-party firms to certify that their food safety control processes meet acceptable standards. Third-party food safety certifiers examine suppliers for compliance with both microbial quality control processes and pesticide application and residue regulations.

Use of returnable containers/pallets. These include recyclable plastic cartons (RPC's) and standardized pallets. They reduce solid waste and may help to streamline physical handling at the distribution center and store levels.

Develop special packs. Buyers often have needs for particular size, quality, and variety configurations, and suppliers may be asked to customize product offerings to meet these needs.

Electronic data interchange (EDI) or retail link programs. These electronic exchanges are bilateral between specific retailers and their preferred suppliers. They may be used only for invoicing or for electronic ordering and other procurement activities.

Provide private labels. The demand for customer-specific labels is growing, both among retailers and distributors. These help to differentiate firms relative to their competitors.

Automatic inventory replenishment. The supplier is electronically integrated into the buyer's inventory management system. The preferred supplier thereby has the responsibility, authority, and access to the data necessary to co-manage the inventory with the retailer, according to negotiated parameters. The supplier is responsible for maintaining appropriate inventory levels at identified distribution centers and for shipping product according to their agreement with the buyer, rather than waiting for product orders from the buyer.

Special merchandising displays. Special merchandising displays may enhance product sales. Suppliers may assist retailers in designing and putting in place displays aimed at stimulating consumer demand.

Category management. The process of making data-based decisions on shelf allocation, product mix, pricing, and merchandising strategies within a category of products, with the goal of improving category profitability. To conduct effective category management there must be access to accurate retail data at the product level. Retailers may conduct category management independently, in conjunction with their supplier partners, or with industry-wide representatives, such as commodity marketing commissions. More shippers are investing in the analytical and information management capabilities necessary to provide this sophisticated service to customers.

being implemented by many commodity shippers. As such, many firms were unable to estimate the ultimate cost. The recent rapid growth in the use of this certification is largely due to several national chains beginning to require this service of their fresh produce suppliers. While a 71-percent compliance rate was reported, only 37 percent of shippers viewed it as beneficial. Nevertheless, food safety certification services are likely to quickly become the norm as most shippers indicated that they would be implementing certification programs in response to changing buyer preferences.

Most, if not all, of the interviewed lettuce and bagged salad firms had requests from retailers for third-party food safety certification. A few of these shippers had been using third-party certification for a decade or more. Others had developed inhouse food safety programs. Some of those with their own programs view third-party certification as redundant and unnecessary, particularly when the standards and suggested certifiers differed among retailers. Only one of the firms had not complied with the request for third-party certification. Opinions on the impact of third-party certification differed among shippers. Six lettuce/bagged salad shippers considered third-party food safety certification as beneficial and three considered it harmful.

The use of ***returnable plastic containers (RPC's) and pallets*** had the second highest request rate at 69 percent, as well as the second highest compliance rate of all service types at 83 percent. Most shippers consider the service to have either a neutral or beneficial impact. In the United States, the use of RPC's is most common with mass merchandisers, although they are commonly used in Europe. Their use is expected to increase, and some shippers felt that their ability to provide these services gave them a competitive advantage.

The issue of ***special packs*** can be controversial. Some firms provided special packs only when they were sufficiently compensated to avoid a net cost. In other cases, shippers felt pressured to provide costly packs for which they felt they would be insufficiently rewarded, with a third losing accounts over their unwillingness to provide the service (table 15). One national chain recently adopted a standardized stackable box for most fresh produce to facilitate internal materials handling and reduce costs. This could have significant cost implications, especially for shippers packing in sheds (as opposed to packing in fields) because it can entail changing bandwidths and other costly adaptations. For large shippers, these costs could be hundreds of thousands of dollars. Furthermore, the standard carton proposed might not suit all crops from a postharvest handling perspective. Issues of this type are likely to become more contentious.

Electronic data interchange (EDI), or retail link program, is another service where the experience of commodity and fresh-cut firms differed. While EDI systems had been requested of 56 percent of the firms, most reported that even though they were set up to use it based on the requests of specific buyers, the buyers never successfully implemented the system. EDI is more important for lettuce/bagged salad firms; 92 percent of the firms had offered or had been asked to use EDI and 83 percent of the requests had been complied with. All bagged salad-only firms used EDI, with several indicating they offered EDI to their customers. The more commodity-oriented shippers waited for customers to ask for the service. Bagged salad shippers generally viewed the impact of EDI as either neutral or beneficial. For other commodities, a significant share of firms is EDI-ready if buyers do decide to incorporate it into their procurement practices.

The use of ***private labels*** appears to be on the rise, requested of 48 percent of shippers, with 65 percent of the requests reported to be new. Some firms might only supply an account or two with private labels while others relied more heavily on this marketing strategy. While 81 percent of the requests were complied with, 60 percent of the requests not complied with resulted in at least one lost account.

In general, shippers felt that the growing buyer interest in private labels was beneficial or had a neutral impact on their business, with only 25 percent describing the trend as harmful. Again, the impact varied across commodities, with 100 percent of grape shippers considering them to be beneficial and orange shippers more ambivalent. This could be due to the practice of some retail/mass merchandiser buyers designating buying brokers to handle their orange sourcing. In these instances, the buying broker may sell its private label to the retailer and charge the shipper a per-box fee for the use of the private label. Shippers maintain that they are only selling through the buying broker because the buyer requires it and that they would otherwise sell directly to the retailer and avoid the private label "licensing" fee. As European chains increase their presence in the U.S. market and more buyers implement supply chain management, the use of private labels is likely to increase. The direct use of private labels by chains may not involve licensing fees.

More fresh-cut products are also showing up on store shelves with private labels. According to IRI data, supermarket sales of private-label bagged salads have risen from 2.4 percent of national bagged salad sales in 1994 to almost 10 percent in 1999. A couple of the bagged salad firms interviewed indicated a conscious shift from their own branded product to private label processing and sales—for both retail and foodservice. In metropolitan areas where incumbent bagged salad firms already enjoy relatively large retail market shares, a firm with a smaller market share may find that private labels are a lower cost alternative to introducing and promoting their own branded products. In addition, retail chains are usually more willing to devote some refrigerated shelf space to their own private label. One shipper expects that retail consolidation will contribute to further growth in private-label use as chains sell their private-label products in their acquired divisions.

Automatic inventory replenishment programs are relatively new; 90 percent of requests were new in the last 5 years, with only 35 percent of the firms having received requests to provide this service (table 15). The requests for automatic inventory replenishment reflect its use among mass merchandisers rather than conventional retail buyers. Shippers complied with 84 percent of requests, the highest compliance rate of any service type.

An automatic inventory replenishment program grants shippers direct access to current sales information. Usually, shippers can only monitor sales of their product after the fact with scanner data compiled and sold by national purveyors of data such as Willard Bishop's Fresh Facts and IRI. Commodities have price look-up (PLU) codes, and most fresh-cut products and all bagged salads have universal product codes (UPC) that are scanned at retail. Three out of seven lettuce shippers and all bagged salad firms were requested to provide automatic inventory replenishment and all com-

California Oranges

The California orange industry is oriented toward the fresh market, in contrast to Florida, which produces almost entirely for the processed market. California production totaled 2,513,000 short tons for the 1999/2000 season (one year after the 1998/99 freeze season) compared to 2,677,000 in 1989/90, the season prior to another major freeze. The juice market provides a secondary market for the industry when there are production problems or low fresh-market prices. In 1997/98, 80 percent of production went to the fresh market. During the 1998/99-freeze season, only 57 percent of production went to the fresh market.

The California orange industry ships year round. Navels represent approximately two-thirds of California's orange volume and were traditionally shipped mainly from November to May, with Valencia oranges produced in the late spring through fall. However, grower efforts in the 1990's to target early and late markets mean that the navel season is increasingly encroaching on both ends of the Valencia season. For our sample, the share of navel and Valencia oranges remained virtually unchanged over the period studied with about 74 percent and 26 percent respectively. Many California orange shippers are diversified only within the citrus category. Still, the interviewed firms included some well-diversified shippers for which oranges were not the main product.

The California orange industry is affected by a market structure different from most other commodities, due to the Sunkist cooperative, which has held a 50-55 percent market share in recent years. Several other shippers participate in an information-sharing cooperative called the Central California Orange Growers Cooperative (CCOGC), currently consisting of eight shippers who each market independently. Sales of this group are equivalent to about 25-30 percent of California orange volume. CCOGC does not handle or market oranges, although it does establish a floor price for the volume sold by its shipper members. No sanctions are imposed, however, on its shipper members for sales under the minimum price. In addition to these two cooperatives, there are two large branded players and numerous other independents, with 39 shippers of all types in the 1999/2000 season.

Structural change at the retail level does not always imply consolidation at the shipper level. The orange industry is much less concentrated than it was in the 1960's when Sunkist accounted for almost 90 percent of the volume of California oranges marketed. Independent shippers have gradually made inroads into the California orange industry at the expense of the market leader, with 39 shippers today up from 32 in 1990. Growth of independents may have accelerated since the demise of the orange marketing order in 1994.

While the number of orange handlers has increased, the number of California citrus growers declined from 7,452 in 1977 to 6,768 in 1987 and 4,842 in 1997, the last year in which a referendum was held for the Citrus Research Advisory Board. Some industry experts feel that there may be some double counting of growers in these numbers due to registrations by individual parcels rather than total grower operations, with the total possibly closer to 2,500.

Recent problems in the export market for California oranges, due both to the economic problems in Asia and growth in competing exporting regions, plus long-term stagnation in domestic per capita fresh orange consumption (14.7 lbs. per capita in 1976 compared with 14.9 in 1998 and 13.5 lbs. forecast for 1999/2000), have combined to create excess supply. Growers cite competition from more fruits being available year-round as one of the factors contributing to declining domestic per capita consumption. In addition, the need to peel and section oranges may make some consumers view them as less convenient fruit choices.

U.S. consumers have a preference for seedless navels over Valencias, yet in the past Valencias were the only option offered by the California industry during the summer, helping to ensure a market. As of the 2000 summer season, many retailers were choosing to source southern-hemisphere navels instead of switching from California navels to Valencias. This makes Valencias even more dependent on export markets than normal. The evident preference of many retailers for summer-season seedless varieties, now that this alternative is available, has caught the California industry by surprise. Navel oranges are also facing competition from winter imports of Spanish clementines and oranges. If imports continue at these levels in the future, it is likely that more orange shippers will market imports themselves, as in the case of grapes.

More than half of the interviewed orange shippers reported lower profits in the last 5 years. However, none of these firms reported strategic alliances, joint ventures, or mergers during the same period. Since the time of the interviews a key merger occurred and the trend towards consolidation now appears to be underway and is expected to continue as supply and demand adjust.

plied. Several of those firms did mention additional staff and equipment costs associated with inventory replenishment. On the other hand, firms generally viewed this service as beneficial since it enabled them to more fully participate with the buyer in managing the supply and marketing of their products.

Special merchandising displays are sometimes requested for promotions to enhance product sales. Only 30 percent of shippers had received requests for this service but compliance was high at 80 percent as firms tended to feel that it might stimulate sales. Still, this type of service is much more routinely provided by other types of food industry suppliers, compared with produce shippers. As more produce shippers become year-round, larger suppliers, the economic return on providing this type of service will increase and both retailers and shippers may be more interested in collaborating in this area.

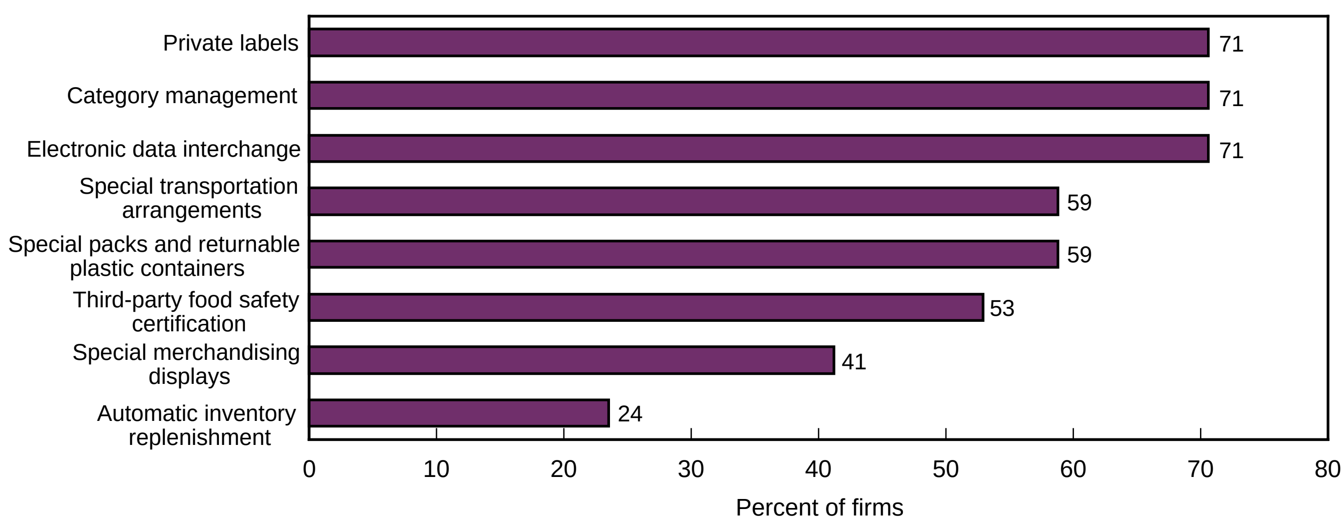
About 28 percent of shippers received requests for assistance with ***category management***, and 80 percent of the requests were complied with (table 15). No one reported losing business if they did not comply. This is a relatively new service, with 80 percent of the requests reported as new in the last 5 years. Commodity produce shippers have generally not been (directly) providing many of these marketing support services, commonly provided to customers by most food industry suppliers, since industry-level generic marketing and promotion programs support many fresh produce commodities. Until recently, category management in fresh produce was hindered by the lack of standardized PLU codes. Category management services are now being offered more often, but still mainly at the generic rather than the shipper level, with the exception of branded products such as bagged salads. In contrast to the commodity shippers, not only did most of the bagged salad shippers offer category management to their customers, some firms specifically mentioned category management as a way to provide top-quality service to their customers.

Retailers Report on Their Requests for Services

Nine out of ten retailers requested more services from their suppliers in 1999 than they did 5 years before. The primary benefit of these services, as viewed by retailers, was better distribution efficiencies and increased overall profits (by reducing the cost of goods sold).

Retailers requested, on average, 5.5 different types of services from suppliers. Almost three out of four retailers are asking suppliers for support in three areas: provision of private-label produce, category management, and EDI (fig. 4). Over half the respondents are requesting special transportation arrangements (such as discounts on transportation for large volume sales), new types of packaging, and third-party food safety certification. Shipper and retailer responses regarding the prevalence of different types of services is less consistent than for fees.

Figure 4
Share of retailers receiving various types of services in 1999



Source: Economic Research Service, Produce Marketing Study interviews, 1999-2000, USDA.