TOWNSEND
and
TOWNSEND
and
CREW
LLP

Denver, Colorado
Tel 303 571-4000

Palo Alto, California
Tel 650 326-2400

Seattle, Washington
Tel 206 467-9600

San Francisco

Two Embarcadero Center
Eighth Floor
San Francisco
California 94111-3834
Tel 415 576-0200
Fax 415 576-0300

June 22, 2000

VIA FEDEX

Mr. Donald S. Clark
Office of the Secretary
Federal Trade Commission
600 Pennsylvania Avenue, N.W.
Washington, D.C. 20580

Re: Comments Regarding Slotting Allowance and Other Grocery Marketing Practices

Dear Mr. Clark:

I understand that the Federal Trade Commission conducted a workshop recently on the legality of slotting fees. In the last two years, I have learned about the serious harm which slotting fees have caused consumers and small businesses and in this country. I represent a plaintiff in a lawsuit stemming from the nationwide imposition of exorbitant slotting fees on wholesalers of magazines by large retailers beginning in 1995. (Cal West Periodicals, Inc. v. ETD, et al., San Francisco Superior Court No. 999793). If appropriate, I hope you will consider the following and the enclosed materials as part of your record in this matter.

The arrival of slotting fees in the market for the wholesale distribution and sale of periodicals transformed this industry overnight. Retailers, along with the few dominant magazine wholesalers that remain in business, have used these fees to destroy hundreds of small businesses and cause substantial harm to consumers – in the last few years magazine prices have substantially increased and the output of magazines has significantly been restricted.

Five years after the industry-wide slotting fees agreement between magazine retailers and wholesalers began, the results are clear. The winners: (1) Supermarkets and other large retailers – which have obtained hundreds of millions of dollars in up-front "slotting fees" as well as substantially increased revenue from their portion of the magazine price increases from checkout sales; (2) The four remaining national wholesalers-Pattison/The News Group, Anderson News, Hudson News and Levy – which have obtained 90% market share and now control distribution of magazines in most parts of the country.[1] These wholesalers have paid hundreds of millions in slotting fees and are now beginning to recoup their losses by, among other things, forcing magazines price increases. The losers: (1) Consumers – who have paid and will continue to pay

[1] For example, Hudson dominates the market for the wholesale distribution of periodicals in the Northeastern United States, Levy dominates in the Midwest, Anderson in the Southeast/Southern California and Pattison/The News Group in the Northwest.

substantially increased magazine prices because of these unlawful slotting fee agreements. Consumers also have been and will continue to be injured because the few remaining wholesalers are restricting the number of titles they will distribute and decreasing or eliminating services to smaller retailers; (2) Small businesses (including especially small wholesalers like Cal West) – approximately 200 of which were put out of business by the retailers' decision to extract slotting fees from wholesalers. Also, many small retail magazine sellers have lost their supply of magazines or significantly decreased services from the few remaining wholesalers who have had to focus their efforts on supplying supermarkets and their other large retailers customers; (3) The small publishers/distributors of new or niche magazines which will have difficulty gaining access to wholesaler distributors and/or have incurred prohibitively increased costs imposed by the few wholesalers which control the chain of distribution.

The harmful effect of slotting fees on consumers is dramatically enhanced by one unique aspect of this industry: Magazines, unlike many other products sold in supermarkets, are priced, not by the supermarkets, but by the magazine publishers/distributors which print prices on magazine covers. It is apparent that, because of their control of the distribution channel and their need to recoup the hundreds of millions of dollars they have paid to retailers in slotting fees, the remaining magazine wholesalers have essentially forced some or all of the five major magazine publishers/distributors (Time/Warner, Hearst Corporation, Murdoch, Curtis and Kable) to increase magazine prices. Because retailers have also traditionally received approximately 30% of the newsstand prices for magazines, these increased prices have also substantially increased the "checkout profits" of retailers from magazine sales. Furthermore, retailers have not passed to consumers any savings from their slotting fee agreements. Indeed, supermarkets have garnered the astounding gross profits from these slotting fees from wholesalers while at the same time forcing consumers to pay substantially more for magazines.

I have enclosed a copy of the complaint in the Cal West Periodicals matter. For your convenience, I will briefly summarize the allegations: The plaintiff, Cal West, was a privately owned wholesaler of magazines which delivered magazines in Northern California for 60 years. The defendants in our action are eight entities that operate on two different tiers of the distribution industry. Four defendants – East Texas Distributing, Inc. ("ETD"); Aramark Magazine and Book Services, Inc.; Anderson News Corporation; and The News Group, Inc., dba The Jim Pattison Group (collectively the "Wholesaler Defendants") – are or were periodical wholesaler/distributors. The latter two wholesalers, Anderson (which purchased Aramark which itself earlier had purchased ETD) and Pattison, represent two of the remaining four major wholesalers in the United States. The other four defendants – Lucky Stores, Inc.; Safeway, Inc.; Raley's; and Host Marriott Services USA, Inc. (collectively the "Retailer Defendants") – are companies that engage in the retail sale of periodicals to California consumers. We allege that for the first time, beginning in mid-1995, major retail supermarkets throughout the country decided to put magazine services up for bid which required that periodical wholesalers pay "slotting fees" totaling millions of dollars to the supermarkets in exchange for agreements to supply periodicals to these stores. Retailers solicited these agreements knowing that they would result in grossly below cost sales by the wholesalers. Moreover, the slotting fees required by these retailer/wholesaler agreement had no relation to any value provided by the retailers since wholesalers stock and service these retailers' magazine shelves. The larger wholesalers agreed to such contracts because they knew smaller wholesalers like Cal West would be unable to compete with their unlawful below cost sales and would ultimately go out of business. We also have alleged that the few remaining wholesalers have now begun to recoup their enormous loses by driving up the newsstand magazine prices and by restricting the type and amount of magazines they distribute.

We sued under California antitrust and unfair competition laws but the conduct described above also plainly violates FTC § 5 and 15 U.S.C. § 13 (The Robinson-Patman Act). Our case is in the early discovery stages. Unfortunately, we have a protective order in the case which precludes me from disclosing some of the information we have discovered. I therefore have enclosed some documents from Cal West's files as well as a few articles from public sources, including issues of the industry newsletter "The New Single Copy," which confirms the substantial harm to competition – including by dramatic price increases and output decreases – caused by slotting fees in this industry.[2]

I believe the FTC should consider investigating the effect on slotting fees in the magazine industry. Not only could your agency force retailers to disgorge hundred of millions in ill-gotten profits from retailers, it could also send a message that the imposition of slotting fees on other supermarket products will be carefully scrutinized. There also may be broader conduct remedies which the Commission could consider including banning retailers from extracting slotting fees when a manufacturer sets an inflexible retail price because any benefits of such fees cannot be passed on.

I thank you for your attention to this important issue. If you have any questions about Cal West or our knowledge of the magazine industry, I would be glad to meet or talk with you at anytime.

Very truly yours,

Paul F. Kirsch by RAM

Paul F. Kirsch

PFK/exs
SF 1100416 v1

---

2 I have highlighted these documents for your review. Also, you will note that retailers and the remaining wholesalers euphemistically refer to increased competitiveness or efficiencies brought about by slotting fees in this industry. However, the facts – increased prices and decreased prices of magazines – belie their spin.