



## EDITORIAL

# ARE DEALER AGREEMENTS DEAD?

**A**s reported elsewhere in this issue, MARS, the 28-store chain, recently swapped an estimated \$16 million (retail value) of inventory for advertising credits with Active Media, a barter firm. Active Media in turn sold the inventory to Digibid, an online auction site, where it is now being sold off to the highest bidder. (See page 58 for more details.) An inventory dump of this magnitude was obviously not a part of the ambitious MARS growth plan. More ominously, however, it poses a serious threat to the health of the industry's distribution channel.

Amidst the legal boiler plate about maintaining a "representative stock," "providing adequate service levels," and "making a best effort" to promote a given product line, all of the dealer agreements we have reviewed contain a clause that emphatically prohibits a retailer from selling merchandise to another retailer or reseller. The purpose of this language was to limit transshipping, which, although prevalent among retailers, typically involved small transactions. In shipping several dozen truck loads of inventory to a barter/liquidator, MARS has not only pulled off the largest transshipping deal in industry history, it has also apparently flouted scores of dealer agreements.

Since news of MARS' monumental blowout broke, we have been besieged by calls from irate dealers across the country. Their uniform complaint is straightforward and compelling; "If a big dealer like MARS can ignore dealer agreements, what right does a manufacturer have to ask me to sign and abide by a contract?" With numerous dealers, both large and small, asserting they will never sign a dealer agreement again, we worry that this controversy could lead to total distribution chaos and a consequent decline in industry prosperity.

To effectively serve the market, m.i. retailers have to make a much larger inventory commitment than most other retailers. (While m.i. retailers aim for a 3 time inventory turn, hardware stores routinely achieve a 7 time turn, and a 6 time turn is common among consumer electronics retailers.) Suppliers

concur that the main purpose of dealer agreements has been to curtail "free-riding" dealers, those who carry no inventory and offer low-ball pricing, so that "authorized" retailers have the incentive to invest in the inventory and service necessary to build the brand. If a smattering of small storefronts across the country offering goods at a few points above cost pose a threat to "authorized" dealers, then what about Digibid.com, where prime merchandise is being offered at hundreds below dealer cost?

The MARS/Digibid situation presents industry suppliers with a difficult question: Are dealers who invest in inventory and service important, or should distribution be turned into a free-for-all where anything goes? Alternatives may develop in the future, but at present, well stocked and staffed stores remain the most effective vehicle for a supplier to present products to the buying public. In the absence of these stores, it's hard to see suppliers faring well at all. The issue is further magnified by the explosion in e-commerce. As we write this, major consumer electronics retailers are in an uproar because Amazon.com is blowing out 33 top-selling Sony products. What would stop the online giant from adding a few prime m.i. items to its offerings? If dealer agreements are effectively null and void, the answer is nothing.

The big chains demand extra discounts from suppliers arguing that with their massive stores and extensive marketing, they provide more support than independent dealers. Suppliers scanning the blowouts on the Digibid.com site must be asking themselves, "Is this the kind of support those extra discounts got us?" MARS officials declined to comment on this transaction, but we'd be interested to know how it fits in with their stated mission of "expanding the market." Most importantly, we hope that suppliers don't allow short-term considerations to undermine a distribution network that has served them well for decades.

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Editor