

FEATURE

EAS SOURCE TAGGING 20-PLUS YEARS OF INNOVATION PART 2

By Robert L. DiLonardo

Every so often, a simple idea catches the imagination, fervor, and engagement of a group of people and is developed into a successful practice that revolutionizes a business. Electronic article surveillance (EAS) source tagging is definitely one of those.

In Part 1 of this two-part article in the January-February edition, we looked back at the beginning of this story in 1994 when The Home Depot executed the first contracts for EAS labels affixed directly by manufacturers in their packaging, rather than by in-store labor.

At that time there were three companies jockeying for control of this segment—Knogo, Sensormatic, and Checkpoint. Each marketed different technologies, which motivated retailers to push for a single industry standard, which is where the second half of this story begins.

Attempts at a Standard

In those early days, none of the EAS manufacturers wished to cede its technology to an open standard; even if theirs had been selected. Each wanted to control its own destiny, maximize the value of its advantages, and capture the entire market. But there were attempts by various retail trade groups to obtain a consensus on a single standard within specific merchandise categories.

National Association of Recording Merchandisers. The first of these efforts was organized by the National Association

“In the market where it was tagged and accessible, the sales rate was much greater and the shortage was virtually nonexistent. It certainly proved our point to the manufacturer that source tagging will both increase sales and reduce shoplifting.”

King Rogers, then vice president of asset protection for Target as quoted in a 1993 *New York Times* article after a four-month store test.



of Recording Merchandisers (NARM). A couple of direct quotes will give a sense of the tension level of the times.

“In 1987 the original NARM source-tagging committee was poised to recommend electromagnetic (EM) technology as the standard. Before this recommendation was adopted, the committee was made aware that the maximum width between pedestals using EM technology was 34 inches, and that most mall landlords would prohibit the installation of multiple pedestals at a store front. This near faux pas caused NARM to form a new loss prevention committee...whose charter was to evaluate the feasibility of selecting a single EAS technology. It was at this point that I began

my twelve-year odyssey and participation in working to achieve the source tagging of prerecorded entertainment products.” Excerpt from “How EAS Source Tagging Rewrote Shrinkage History in the Music and Video Sector” by O. Keith Wanke in the May-June 2002 edition of *LossPrevention* magazine.

“Their product wasn’t picked, so now they’re doing a lot to try to sabotage our effort.” Quote by Michael E. Pardue, former chief operating officer at Sensormatic in a *New York Times* article titled “Putting the Tag on Shoplifters” published in May 1993.

In the late 1980s music retailers were major users of anti-theft devices. Their merchandise was desirable, easily concealed and the customer base included shoplifters. Much of pre-EAS security involved cardboard “longbox” packaging. Facing pressure from ecologists, the industry agreed to eliminate them by April 1993. A move toward source tagging was a logical solution.

In preparation for the longbox conversion, NARM tested EAS systems with the intention of establishing a standard. Of the four participants in the testing—Checkpoint, Sensormatic, 3M, and Knogo—only Checkpoint was wedded to a single technology—RF. The others, especially Sensormatic, could more easily adjust if NARM ruled out AM or EM in favor of RF. Thus the stakes for Checkpoint were extremely high, even though it was likely that the winner would license its technology to the other companies.

As 1992 ended, NARM’s decision was imminent, but its announcement delayed. Checkpoint released a full-page ad in the January 9, 1993, issue of *Billboard* magazine claiming that certain magnetic deactivation systems could distort the audio quality of audio and videotapes. While Sensormatic was not named in the ad, the AM technology it criticized was proprietary to Sensormatic, and based on NARM’s published selection criteria was the only logical alternative to RF. Sensormatic immediately filed suit against Checkpoint for false and misleading advertising, seeking \$35 million in damages.

In February 1993 rumors that the NARM subcommittee had recommended the Sensormatic system sent Checkpoint stock tumbling, losing a third of its value in two days. Then, in March NARM announced its decision to go with Sensormatic's AM, only to discover through further testing that the system's deactivation process did, indeed, cause deterioration in the sound quality of some lower quality "Type 1" cassettes.

The news sent Sensormatic's stock down, while Checkpoint's rebounded. While Sensormatic rushed out new deactivation devices that it maintained corrected the issue, Checkpoint again trumpeted the studies that led to the original suit, as it tried to pressure NARM to reopen its selection process. But the decision stood.

NARM's selection of AM established the technology as the standard for the entire record industry and by implication for the mass merchants, discounters, drugstores, and other retailers what sold cassette tapes, compact disks, and related products. The stakes were high indeed.

On June 26, 1993, Sensormatic agreed to drop its suit against Checkpoint, when the companies agreed not to criticize one another in advertisements. As part of the settlement, however, Sensormatic discontinued its agreement to sell Checkpoint products in Europe. The next month, to forestall a loss in European sales, Checkpoint acquired Dutch makers of security products and services, ID Systems International B.V. and ID Systems Europe B.V.

The NARM controversy continued to fester in the marketplace. Checkpoint and Target Stores, an RF EAS user

and high-volume seller of music products, filed an anti-trust lawsuit against NARM. In 1996 when PolyGram Group Distribution began to source tag according to NARM recommendation, Checkpoint and Target sued them as well.

In August of 1996 a court dismissed several of those lawsuits in exchange for PolyGram's voluntary suspension of its source-tagging operation, with the duration of the suspension to be determined solely by PolyGram. PolyGram's President James Caparro said at the time, "We are confident our method of analyzing and choosing the available technology was well-executed and clearly within the law. While we are still convinced about the merits of source tagging and committed to EAS implementation, we are adopting this temporary suspension in light of the confusion and friction which followed our announcement." Caparro noted that PolyGram retained the ability to adopt any program it deemed in the best interest of the company.

The settlement of the lawsuit did not change NARM's recommendation of the AM technology. The music distribution companies still needed to embrace source tagging immediately and work with other NARM members who were not AM users to facilitate source tagging with the technology of their choice.

Consumer Products Manufacturers Association.

Toward the end of the 1990s, there was another organized attempt to establish a global standard under the auspices of the Consumer Products Manufacturers Association (CPMA), founded in 1999 by Eastman Kodak, Johnson and

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Johnson, The Gillette Company, and Procter & Gamble. The stated purpose of the association was to provide focus to the evolving needs of products and product packaging in three areas—electronic article surveillance, product authentication, and identification.

The membership believed that global standards were critical to establishing an efficient response to incorporating new technology in the market place. Hindsight proves that a standard would have been beneficial. Unfortunately, by this time the competing EAS technologies had successfully grown well beyond critical mass, and the EAS vendors were still unwilling to relinquish the control they had amassed.

In the late 1990s, the CPMA proposed that the consumer packaged goods (CPG) industry consider both a “tag-centric” and a “tower-centric” approach to developing a global consensus for product security in retail. The adoption of a single standard would simplify the source-tagging and inventory-management exercise for manufacturers, reduce costs, and result in more manufacturers’ cooperation with source-tagging initiatives.

“We organized many meetings, including the RF source-tagging conferences with retailers, manufacturers, and packagers. It took some ‘arm twisting’ by the retailers for manufacturers to appreciate their opportunity because they made money on reorders generated from theft.”

Dave Shoemaker, former group vice president responsible for source tagging with Checkpoint.



The first idea was to develop some performance-based standards around the tag. Besides the EAS component, this tag would contain anti-counterfeiting properties, such as a hologram, and would accommodate the future inclusion of RFID. For CPG manufacturers and packagers, tag-centrism would be ideal because it would supply all security needs with a single style of tag, rather than having to supply the appropriate EAS technology on a customer-by-customer basis. *But*, retailers would not be free to choose the type of EAS pedestal technology that best suited their needs. Tag-centric meant selecting one of the three current EAS technologies as a standard. As discussed in Part 1, retailers choose a particular EAS technology *because* of the unique benefits provided by a technology. So, this idea quickly turned into a “dud.”

In August 1999 the CPMA changed tactics and proposed the industry take a “tower-centric” approach to the problem. A tower is the CPMA’s jargon for an EAS

pedestal. Tower-centrism means one EAS system detects all tags, irrespective of technological base. While, the CPMA acknowledged that each of the EAS tag technologies can demonstrate superiority in combination with certain types of packaging, they suggest, by an extension of logic, that a single EAS system containing multiple technologies would allow merchandise manufacturers and packagers the opportunity to insert the best, most cost-efficient EAS tag into the item. This idea was completely unfeasible—worse than the first—and also died a quick death.

“Dual technologies made progress difficult. It gave the consumer-product manufacturers an excuse not to engage at the beginning,” said Kevin Dowd, former president and CEO of Checkpoint.

Many people in the EAS industry agreed with Dowd, and thought that the CPMA was organized as a tactic to delay participation in source tagging as long as possible. Once the industry figured out how to identify and measure the benefits for all constituencies, and realized that a single standard was already too late, everyone just got to work.

Early Adopters and Landmark Customers

In the beginning there were willing, even anxious early adopters among EAS vendors and retailers. Intrepid, enlightened merchandise manufacturers took risks in exchange for more visibility, including Black & Decker, Texas Instruments, Victorinox Swiss Army, PolyGram Group, Rayovac, Pfizer, and Estwing Manufacturing to name a few. Here is a sample of the early action.

Checkpoint. In the late eighties Checkpoint announced formal efforts to develop and promote source tagging. It took several years, but under Ted Wolf’s vision, leadership, and focus, the marketing team stimulated two small-scale tests. One situation evaluated a new product idea, while the other blossomed into a landmark chain-wide rollout for the Checkpoint source-tagging program.

continued on page 44

continued from page 42

Tools Plus, a Waterbury, Connecticut, hardware store, tested Checkpoint's "activatable" label in 1991 in collaboration with Black & Decker. At that stage Checkpoint had yet to perfect the RF label roll formatting that would withstand the rigors of a high-speed source application process. "Tagging killed 70 percent of the labels," recalls Checkpoint's Seth Strauser. "So we disabled the label during the application process and provided an activator to turn it back on once it arrived in the store." This concept proved workable for some retailers, but large-scale demand for this type of product never materialized in the marketplace.

The landmark deal incubated during the same year with a test in a 60-plus store, Detroit-area hardware chain called ACO Home & Garden Hardware. Bill Aiken, the CEO, immediately grasped Checkpoint's vision and was convinced that source tagging would be a "game changer" for his organization. He solicited Victorinox Swiss Army to collaborate on a test that featured tagging in ACO's distribution center. On the strength of the results, ACO gladly took a very big risk and agreed to an immediate EAS rollout

The test ran four months. When interviewed in 1993 by the *New York Times*, Rogers said, "In the market where it was tagged and accessible, the sales rate was much greater and the shortage was virtually nonexistent. It certainly proved our point to the manufacturer that source tagging will both increase sales and reduce shoplifting."

Academics might opine that the Target test sample was statistically insignificant, but the methodology has become extremely important to the retail loss prevention industry in the big picture. Just look at the groundbreaking work that the Loss Prevention Research Council and others have done over the past few years.

Checkpoint considers The Wiz to be its first full-fledged source-tagging rollout. This New York-based electronics chain reached its peak of 94 stores and about \$1.3 billion in annual sales. The deal was consummated in 1995. There were two key drivers in this effort. The first was efforts by Wiz management to push CD and DVD replicators to affix labels. More importantly to the Wiz, however, was a requirement that Checkpoint figure out a way to integrate scanning and deactivation, which they did.



"The initial high-risk, source-tagging targets were cameras, film, consumer electronics, and recorded media. Shrink reductions were so positive in electronics that management said 'let's accelerate the rollout to twenty-four months,' which we did with the help of second-tier suppliers who grabbed an opportunity to secure more shelf space."

Jeff Powers, former global account manager responsible for Walmart at Sensormatic.

in all stores, with the intention to source tag further back in the manufacturing process. After years of work honing the sales pitch and developing the program, Checkpoint had found the formula. More success followed quickly.

Target Stores, under the capable guidance of King Rogers, then vice president of asset protection, conducted a landmark test in 1992 that included a small, randomized control trial with a formal analysis of the economic benefits of source tagging. Target and Texas Instruments (TI) wanted to find the best way to secure hand-held calculators without resorting to locked fixtures that would inhibit sales. They collaborated on a three-store test in which TI inserted RF EAS labels into the packaging of two types of calculators to be displayed on open peg hooks in a Detroit store. An Indianapolis store was the control, where calculators were hung on peg hooks without EAS tags. A Minneapolis-area store was set up with untagged calculators under glass and lock and key.

Over the next couple of years, Checkpoint announced other chain-wide rollout deals with Eckerd Drug Stores, Rite Aid, Walgreens, Thrift Drug, and Big V Drugstores, covering high-risk products manufactured by the "who's who" of consumer-products manufacturing. Source tagging with RF EAS had more than reached critical mass.

The Eckerd Drug Store case introduced new innovations in the way source tagging could be managed. Eckerd's LP department was the first to assign an executive to establish strong working relationships with buyers and the manufacturers from whom they procured merchandise. "The goals were to get everyone to understand the benefits of source tagging," recalls Elliot Rosenblatt, Eckerd's original holder of the position, "and to make certain that the manufacturers understood it was a very high priority of Eckerd's. We had the authority to insist on source tagging, or the product was going behind the counter."

Rosenblatt also used POS exception reporting to help identify the high-loss items to be included in the program. The other innovation was called “fractional tagging,” whereby only every second or third item was source tagged. Labels at this point were mainly concealed on the inside of packaging, so skipping some labels to save cost was worth the risk. Thieves couldn’t tell which items were tagged.

Sensormatic. The first rollouts by Sensormatic also emanated from successful tests. In 1992 Edward A. Wolfe, Home Depot’s vice president of loss prevention, organized a three-store test of AM EAS in tool corrals, where the shortage was “double digit.” After six months, the shortage in the tagged categories dropped by about 80 percent, but losses “migrated” outside of the corrals. Wolfe wanted to expand to exit coverage, but he had some issues to contend with. A couple of them were technology related, but the bigger issue was financial.

Wolfe’s boss wouldn’t allocate a single penny for tagging labor. The potential savings were compelling enough that the boss suggested that Wolfe lobby buyers of high-loss merchandise for support for source tagging. Wolfe knew that the buyers had never collected a bonus based upon their shortage performance. So, he asked for a meeting to offer them a proposition—the promise of a bonus in exchange for support for the program and direct assistance engaging merchandise manufacturers in the tagging process.

“Based on the test results, I was pretty certain that the shortage would drop low enough to earn the bonus,”

Wolfe recalled. “But they agreed.” And his boss did, too. So Wolfe formulated a plan to source-tag 1,500 SKUs. Sensormatic solved the technological issues, Home Depot signed a contract, and the buyers earned their first bonuses.

Around 1994 convincing manufacturers to source tag presented other problems for Home Depot. The inventory shortage in batteries was astronomical, to the point where the category gross margin had to have been breakeven at best. The major brands didn’t see the wisdom in tagging at first. But after an enterprising second-tier brand volunteered, and shelf space allocations were altered in their favor—drastically in a couple of cases—the major brands got the picture. “The battery story certainly underscored the tension as well as the opportunity,” mused Wolfe.

Walmart signed its first contract with in-store tagging with Sensormatic for AM EAS around April 1991, before the introduction of proximity deactivation. In the summer of 1998, Walmart signed a chain-wide rollout agreement with about 500 installations per year for five years. A key ingredient in the sale was the improvements Sensormatic made to its AM label size and performance, and the introduction of improved deactivators called “Rapid Pads.”

“The initial high-risk, source-tagging targets were cameras, film, consumer electronics, and recorded media,” said Jeff Powers, Sensormatic’s global account manager responsible for Walmart at the time. “Shrink reductions were so positive in electronics that management said ‘let’s accelerate the rollout to twenty-four months,’ which

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we did with the help of second-tier suppliers who grabbed an opportunity to secure more shelf space.”

Kmart signed its first agreement for AM EAS with Sensormatic in 1993. In 1995 the agreement was expanded to include more stores, and the inclusion of Rapid Pad II proximity deactivation to facilitate a future move toward source tagging. In late 1996 Kmart and Sensormatic agreed to another expansion covering over 1,000 remaining locations.

CVS, a Sensormatic user since 1987, announced a chain-wide installation of AM and an upgrade to proximity deactivation in early 1996. At that time merchandise manufacturers were source tagging about 500 SKUs for CVS. Plans called for an aggressive expansion of the program. Years later, CVS converted from AM to Checkpoint-supplied RF technology.

As source tagging grew in size and scope, entrepreneurial valued-added resellers fashioned profitable opportunities in support roles. Jobbers, distributors, replicators, and packaging companies affixed labels. Purveyors of retail trim products, such Paxar Corp., Avery Dennison, B&G Plastics, and A&H Company invented disposable products that helped secure source-tagged merchandise. Other entrepreneurial people introduced solutions to specific high-loss situations as they arose.

Knogo. In mid-June 1993, Knogo planned to announce that Sonopress, the manufacturing division of the Bertelsmann Music Group of Germany, had selected two Knogo theft-detection products that would be embedded directly into recorded materials like cassette tapes and compact disks, according to people familiar with Knogo’s plans. One product was the previously mentioned Superstrip, a thin strip that can either be embedded into a product or applied to packaging. The other was a round version specially designed by Knogo for Bertelsmann to fit the center of a compact disk.

The controversy over NARM’s selection of a preferred EAS technology completely overshadowed Knogo’s efforts. Knogo’s non-North American operations were acquired by Sensormatic the next year. The remaining entity, Knogo North America, kept promoting the Superstrip and battled to participate in the source-tagging market for a few more years.

Convincing the Doubters

Consumer-Products Manufacturers. In the beginning the consumer-products manufacturers, in general, saw little vested interest in accommodating source tagging. All the financial metrics were negative for them. The major issues facing them revolved around the money that would have to be invested to design, build, and manage the new tagging processes.

It wasn’t as simple as changing the artwork on the outside of packaging. There were legitimate concerns that the endeavor would have a negative impact upon

Source Tagging Milestones

All-Tag Americas Inc.

- Over 4 billion RF EAS labels sold in support of source tagging.
- Second largest supplier of RF EAS labels in the world.
- Continuous support of global source tagging initiatives since 1995.

Checkpoint

- 1994—First orders for source tagging in over-the-counter drug remedies for Eckerd Drug Stores and Rite Aid.
- 1995—Source-Tagging Evaluation Laboratory opens to all vendors.
- 1997—Introduces EAS integrated jewelry card.
- 2001—Perfects PSG label format technology that matches speeds of production and packaging lines.
- 2003—Launches “sewn in” security for apparel.
- 2005—FDA-compliant products for tagging food and microwave operation.
- 2006—Introduces “postage stamp” size label.
- 2008—Introduces reverse-logistics program called Hard Tag @Source to recycle reusable EAS tags for apparel.
- 2012—Emphasizes “visible tagging” to improve deterrent quality with a lock symbol indicating security.
- 2014—To date over 25 billion products have been source tagged from all sources.

Sensormatic

- 1994—70 million AM labels sold for source tagging.
- 1994—Some of the earliest name-brand manufacturers to begin tagging included Stanley Tools, Bernzomatic, and Estwing for DIY; Schering Plough (Maybelline), Pfizer (Advil), Rayovac, Ever Ready, Magnivision, Kodak, and McNeil (Tylenol).
- 1997—Over 1,000 consumer-products manufacturers and packagers provide source-tagged merchandise.
- 1999—Label unit volume reaches 1 billion per year due to Walmart’s source-tagging ramp up.
- 2000—The focus of merchandise manufacturing shifts to Asia. Source-tagging customers procure and tag in Asia, but ship tagged merchandise to the developed world.
- 2005—The explosion in the sales of DVDs and multimedia merchandise helps drive label unit volume to 4.5 billion per year.
- 2014—To date, over 50 billion products have been source tagged with disposable labels and “sewn in” disposable or reusable visible source tags (VST) on apparel. Over 5,300 manufacturers, packagers, and value-added resellers (VARs) are actively tagging. VST annual unit volume is expected to reach 1 billion.
- Future in apparel source tagging fueled by Auto-ID/RFID applications.

Wallace Computer Services

- 1998—Licensed by Sensormatic to build and sell AM labels for high-speed, automatic applications at a rate of over 1 billion per year.
- 2014—Cumulative label unit volume surpasses 3 billion.

continued on page 48

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continued from page 46

reorder rates. The perceived benefits stream—less theft—was largely hypothetical, unmeasured, hence unproven. The specter of locking up merchandise or losing shelf space was a big decision driver. A positive return on investment (ROI) was little more than an illusion. The list of issues faced by the consumer-products manufacturers was daunting:

- **Costs**—The costs to manufacturers went well beyond just the cost of acquiring the security labels. Affixation costs included investment in design, manufacturing process changes, automated equipment, and labor. Finished goods inventory management and carrying costs included distributing the appropriately tagged merchandise to the retail stores. Given there were four possible stocking permutations for each high-risk SKU—un-tagged, AM, RF, or EM—inventory management was challenging. Could some or all of these costs be successfully passed onto the wholesale cost of the merchandise?
- **Benefits**—The benefits accruing to the manufacturers were hard to measure. In theory less theft means a better “sell through.” A reorder triggered by a sale is “more beneficial” than one triggered by a theft. Providing products with a value add strengthens the partnership between retailer and supplier. A major inducement was the promise of additional shelf space with its immediate impact on sales. Open merchandising opportunities would be either lost or gained. Simply stated, source-tagged items would be open merchandised, while non-tagged products were locked up or threatened with removal.

“We organized many meetings, including the RF source-tagging conferences with retailers, manufacturers, and packagers. It took some ‘arm twisting’ by the retailers for manufacturers to appreciate their opportunity because they made money on reorders generated from theft,” said Dave Shoemaker, former group vice president responsible for source tagging with Checkpoint.

Rebalancing the ROI. For retailers at the time, EAS was far from a unanimous choice as an anti-shoplifting countermeasure. Source tagging demanded a chain-wide rollout, while loss prevention executives were investing their capital in high-risk locations. Microprocessor-controlled CCTV systems were the rage, and a number of retail vertical markets, such as supermarkets, preferred video solutions over EAS.

Source tagging would have failed without net positive economic benefits for all participants. Retailers were losing money without it. Manufacturers were faced with high “buy-in” costs to participate. The economic seesaw needed to be rebalanced. The scenario can be explained this way—Retailers tried to execute their sales plans. They went into the market and bought merchandise, applied an initial mark up, put the goods out for sale, sold some at regular price, marked most of it down, had some stolen, and liquidated what was left.

“The key was in proving the business models and rebalancing the profit sharing for all the

partners,” said Joe Ryan, Jr., former vice president of global source tagging for Sensormatic.

Two things ruined the gross margin for the retailer. First was the replenishment costs added to the inventory by the reorders made because items had been stolen rather than sold. Second was the gross margin hit from the shrinkage reconciled and booked at fiscal year-end. The retailer paid the price, and the consumer-products manufacturers weren’t economically affected.

As retail merchandise statistics got more detailed and reported much closer to real time, the CFO got a better handle on the depth, breadth, and scope of these drains on item-level profitability. The merchants saw this in the form of low gross margin and promptly started negotiating “allowances” to offset shrinkage losses.

Why would the manufacturers agree to forsake the replenishment gravy train and take on a process that had the potential to add significant costs and disruption to production and control of finished goods inventory? As time passed and the data included all the relevant statistics to the SKU level, gross margins were so bad for certain high-risk items that something had to be done. Allowances were rarely sufficient.

Frustrated retailers began to tell their brand partners, “I’m getting killed here. We can’t afford to stock your product anymore. You either source tag, or I’m going to allocate your shelf space to someone who will.” This scenario happened several times in a variety of markets and is a major factor in the ultimate success of source tagging.

The early source-tagging adopters benefitted almost immediately. Far less inventory was stolen and more of the residual inventory was sold without “help” from reorders. Gross-margin statistics improved dramatically. Merchandise was preserved from theft and ultimately sold, relieving the inventory and generating a reorder. The profitable partnership between retailer and supplier was rebalancing. It took the better part of two decades to get this all figured out.

The real beneficiary of this journey is the Auto-ID industry and the retailers pursuing RFID as an inventory-control strategy. They recognized from the outset that RFID required a proven, measureable return on investment for all constituents.

“EAS will be here longer than people anticipate. Source tagging’s history is the roadmap for RFID,” said Powers. ■



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