10

Retail Sales

10.1 INTRODUCTION

Retailers represent the final stage in the journey of apparel from its point of origin to the ultimate consumer. In the United States, the retail apparel industry is large, mature (slow-growing), fragmented, and highly competitive.[1] The retail apparel industry includes the sale of womenswear, menswear, and childrenswear. In 2012, the U.S. retail apparel industry generated total revenues of approximately $339 billion, with womenswear representing the largest segment of the industry.[2] Apparel retailers offer merchandise in various styles (such as contemporary, casual, and formal), for various occasions (such as special occasion, resort, and athletic), and at various price tiers. Retailers often sell both apparel and accessories (such as footwear and handbags) as the consumer dynamics of both product categories are similar. Demand for apparel and accessories is largely driven by general economic trends (consumer confidence, personal disposable income, and consumer spending), population growth and demographic trends, and changes in consumer tastes and preferences.[3]

Prior to 1995, apparel retailers primarily used a single distribution channel: brick-and-mortar retail stores. As a consequence of the visual and tactile nature of apparel, and the consumer's desire to try on apparel products for proper sizing and fit, brick-and-mortar stores continue to be the primary source of retail apparel sales.[4] Yet, the retail apparel industry in the United States has experienced a strategic shift since the mid 1990s, due to greater household access to the internet and the rapid growth of mobile device usage.[5] Increasingly, retailers have adopted e-commerce and mobile commerce platforms, either exclusively or as part of an omni-channel retail strategy that combines a physical presence with an online and mobile presence to deliver a seamless customer experience.[6] This strategic shift has been accompanied by the development of new technologies aimed at enhancing the online shopping consumer experience so that it more closely resembles the in-store experience, and by the introduction of mobile devices and mobile payment systems into brick-and-mortar retail stores.[7] In addition, the growth of the internet has allowed apparel brands to directly access their customers through e-commerce and mobile commerce websites.

Apparel retailers also have been impacted by the recent growth of "fast fashion" companies, principally the Inditex Group (known for its fast fashion brands including Zara and Massimo Dutti), the Arcadia Group Ltd. (which owns Topshop), H&M, and Mango. These companies (which typically are manufacturers as well as retailers) feature a rapidly changing assortment of merchandise reflecting the latest fashion trends, sold at affordable prices, in attractively designed stores. The speed at which fast fashion companies can move their products into stores has induced more traditional retailers to shorten their delivery, or lead, times in order to remain competitive.[8] The high turnover by fast fashion brands, and their ability to quickly replicate runway designs, have also led luxury brands to transition to a "four to six collections" per year model instead of the traditional "two collections" per year model.[9] Luxury brands, such as Burberry, have also begun to offer merchandise for sale immediately after runway shows instead of letting customers wait months for merchandise to arrive in stores.[10]

This section focuses on the major retail distribution channels for apparel in the United States, and the trends that continue to reshape the retail industry.

A. Department Stores

Department stores are large retailers that stock a wide variety of fashion-oriented merchandise (typically tens of thousands of stock keeping units), which is separated into departments and offered to consumers at full price (with seasonal mark downs).[11] Department stores generally can be divided into market segments, with differing levels of customer service, merchandise selection, and store layout dictated by the target market.[12] These market segments include: higher tier department stores (such as Saks Fifth Avenue and Neiman Marcus), which target affluent consumers; upper moderate department stores (such as Macy's and Dillard's), which target mid-range households; and moderate department stores (such as Sears and JC Penney), which target more value-oriented consumers.[13] Department stores also can be divided by the assortment of merchandise they carry: full-line department stores (such as JC Penney), which carry not only apparel and accessories, but also housewares and furniture; and specialty department stores (such as Saks Fifth Avenue and Nordstrom), which focus on men's and women's apparel, footwear, and other accessories.[14] Apparel merchandise typically accounts for more than half of department store sales revenues.[15] Apparel merchandise includes three main categories: fashion merchandise, which has a long lead time but a short selling season and is dependent on shifting customer preferences; basic merchandise (such as underwear), which is relatively stable in style and demand; and fashion-basic merchandise (such as T-shirts with special trimming).[16] Typically, the first floor of a department store, which is high traffic, carries cosmetics, jewelry, hosiery, and other accessories, which are higher margin merchandise. A department store often serves as the "anchor tenant" in a large mall in order to attract consumer foot traffic to other smaller stores within the mall.[17] The size of department stores varies, but some department store chains have flagship stores that can exceed 250,000 square feet.[18]

The U.S. department store industry, which is comprised primarily of national and regional chains, has become increasingly consolidated, with eight department store chains generating approximately 95% of the industry's total revenues.[19] Department store sales in the United States have experienced a significant decline in the last decade, as a result of increasing competition from other retail channels.[20] Accordingly, some department store retailers have refocused their expansion strategies internationally, in Canada (due to its proximity) and in emerging markets, such as China and India, which have growing middle class populations.[21] Some department store retailers (including Saks, Inc. and Neiman Marcus, Inc.) are partnering with e-commerce technology and services companies, such as FiftyOne Global Ecommerce, to offer international customers the ability to shop online in their local currencies, and some department stores are opening international licensed or franchised stores.[22]

In addition to facing competitive pressures, department store sales are subject to seasonal fluctuations, with sales generally peaking during the fourth quarter of the calendar year, which includes back to school and winter holiday shopping.[23] Consumers are increasingly timing their purchases, particularly of luxury goods, to coincide with anticipated seasonal discounts or other promotions offered by department stores as they seek to clear excess inventory.[24] As a result, some department stores are reducing their inventory levels to prompt customers to make their purchases at the beginning of a season, rather than waiting for future price reductions.[25]

As their focus is attracting and retaining a broad base of customers, department stores often offer attractive rewards programs. These rewards may be offered through proprietary credit cards (where the retailer grants the credit), private label credit cards (where a third party grants the credit but the retailer's name goes on the card), and/or loyalty programs. For example, as a member of Bloomingdale's "Loyallist" program, customers receive periodic "Friends & Family" discounts of up to 25% off merchandise in stores or online.[26] Neiman Marcus "InCircle" members receive special promotions or receive "triple points" for in-store purchases on designated days.[27] These programs provide a competitive advantage to department stores as compared to independent retailers, which typically do not have the ability to offer similar benefits to attract customers.

Department store retailers typically use elaborate systems to manage their inventory from initial purchase to eventual sale to the consumer. Department store retailers may use multiple warehouse and distribution centers that ship products to stores in their region as needed.[28] They also utilize sophisticated information systems to manage their operations. These information systems include: point of sale systems to record and process transactions; merchandise planning systems to forecast and allocate merchandise; inventory management systems to monitor inventory levels; and electronic data interchange to process orders.[29]

Department stores typically purchase their inventory from a combination of manufacturers, distributers, and importers. Although department stores often have long-term relationships with particular suppliers, they seldom have formal long-term supply contracts.[30] Department store buyers may use historical sales levels and fashion trends to make inventory purchasing decisions. In addition to carrying a variety of recognized name brand merchandise, many department stores have sought to distinguish themselves by developing their own private label brands carried exclusively in their department stores.[31] Private label products give retailers more control over product quality and typically have higher margins.[32] Private labels, however, must compete with nationally recognized brands, and so require more marketing and advertising support by the retailer.[33] A department store retailer may also differentiate its merchandise by negotiating arrangements with certain nationally recognized brands to supply its retail stores with limited distribution products or specific pieces each season that are available exclusively in its stores.

Although department stores often sell merchandise from different brands under one section, such as women's shoes or men's apparel, department stores also may have "in-store shops", or separate shops within the larger department store, for certain recognized fashion brands. A few luxury fashion brands staff their "in-store shops" with their own sales associates, use their own distinctive marketing concepts and display formats, and sell their products directly to customers. These luxury brands prefer "in-store shops" for their products in order to offer higher levels of knowledgeable service, and to control pricing and discounting strategies. Other recognized fashion brands have separate shops that are more of a collaboration with the department store retailer. In such cases, the brand and the retailer negotiate an arrangement in which the brand may share the costs of special fixtures, and the brand may select the retailer's sales associates who will staff the shop (and may pay some or all of their compensation), but the products are sold by the brand to the retailer, which then resells them to the consumer. These arrangements offer the opportunity for increased sales for the fashion brand and retailer because dedicated sales associates may more effectively monitor inventory levels, display products more appropriately, and offer better customer service. Some department store retailers also use the "in-store shop" concept for their online stores by creating virtual "designer shops." The real estate issues associated with creating "in-store shops" are discussed in chapter 12.

B. Specialty Stores

Specialty stores include retail stores that focus on stocking merchandise "for a well-defined target market" or that "carry the merchandise of one manufacturer or brand".[34] One of the largest specialty retailers in the United States is Gap Inc.,[35] which owns The Gap, Banana Republic, Old Navy, Piperlime, and Athleta brands, and has over 3,000 stores.

Specialty retailers are the most significant sales channel for apparel, particularly women's apparel, and accounted for about a third of apparel dollar purchases in the United States in 2011.[36] To the extent that a specialty retailer targets a narrow market (for example, Abercrombie & Fitch Co. targets fifteen- to nineteen-year-olds, and Chico's targets "forever 39" women), the retailer must monitor the demographics and priorities of its target customers.[37]

Some specialty stores offer "a limited but deep assortment of merchandise" at several price points.[38] Since these specialty stores are focused on a limited range of merchandise, they are expected to provide higher levels of service and knowledge with respect to the range of merchandise offered. For example, Sunglass Hut and Solstice each carry primarily sunglasses; they provide customers with a deep selection, from high-end designer sunglasses to lower priced merchandise, and from casual models to models geared towards sports or active lifestyles.[39]

C. Discount Department Stores

Discount department stores are large, high-traffic stores offering value-oriented pricing on a variety of merchandise such as apparel, personal care products, electronics, groceries (typically other than fresh foods), and household furnishings. Discount department stores typically occupy large spaces (averaging 100,000 square feet) in strip malls.[40] Discount department stores are able to maintain competitive prices through a combination of supply chain management systems, quantity discounts obtained from manufacturers, high turnover rates on products, and lower overhead.[41] In the United States, the discount department store industry is highly concentrated, and includes such major participants as Wal-Mart Stores, Inc. and Target Corporation.[42] According to recent studies, over 80% of American households have shopped at either a Walmart or a Target store.[43]

In recent years, discount department stores have collaborated successfully with luxury fashion designers to reach a broader range of customers and compete with the fast fashion companies. In a typical collaboration, the fashion designer produces a new branded line of apparel or accessories, at lower price points, specifically for a particular discount department store retailer that sells the line exclusively for a limited period of time. These collaborations have been beneficial to retailers by attracting new customers, and have benefitted fashion designers by increasing their revenues and broadening their customer base without negatively affecting their brand image.[44] For example, since 2006, Target Corporation has been collaborating with international designers such as Proenza Schouler, Anna Sui, Kate and Laura Mulleavy, Jason Wu, and Missoni to offer limited-edition apparel and accessory collections. The Missoni collection, launched in September 2011, included 400 items of apparel, luggage, home furnishings, and beauty products priced at between $2.99 and $599, and sold out within a few days.[45] In 2012, Target joined with a department store retailer, Neiman Marcus, to launch a limited edition winter holiday collection, created by twenty-four well-known American designers, to be sold at both retailers. Most discount department stores also sell private-label products that are intended to offer near brand-name quality at lower prices.

D. Off-Price Stores

Off-price stores sell brand name merchandise at discounted prices.[46] Off-price stores generally belong to one of the following three categories, described below: factory outlets, off-price retailers, and retailer-owned off-price stores.

Factory Outlets

Factory outlet stores have evolved considerably from their historical origins. Initially, brand manufacturers opened factory outlet stores to sell their own branded merchandise that either deviated from technical production specifications or remained unsold at the end of a season. These company factory outlets were located near the company's manufacturing facilities, and the products were sold only to company employees at discounted prices.[47] Although company factory outlets began to offer their merchandise for sale to the general public, they remained single-store locations throughout the 1970s.[48] The first enclosed factory outlet center opened in 1980 and was not intended to compete directly with traditional retail malls.[49] As malls comprised entirely of factory outlets began to proliferate in the United States and Europe, manufacturers needed to increase the amount and variety of merchandise available for factory outlet sale. In a significant shift, companies began to produce merchandise styled similarly to their full-price offerings, but with a slightly lower quality, specifically for sale at lower prices in their factory stores.[50]

Off-Price Retailers

In contrast to factory outlet stores, off-price retailers typically buy imperfect merchandise and excess inventory from a variety of full-price retailers and sell them at discounted prices in their own stores. Off-price retailers include Century 21 Department Store, Marshall's, and T.J. Maxx. Off-price retailers are able to maintain discounted prices on merchandise because their business model and buying cycles operate differently than those of full-price retail stores. Rather than buying from manufacturers for each seasonal cycle, off-price retail buyers continually look for merchandise to carry in their stores. As a result of the timing of their purchases, buyers are able to get merchandise that was not purchased on the standard cycle by full-priced department stores or boutiques. In recent years, as exclusively online off-price retailers, such as Bluefly and Overstock.com, entered the market, traditional brick-and-mortar off-price retailers began to embrace e-commerce to remain competitive.[51]

Retailer-Owned Off-Price Stores

Some department store retailers have opened their own off-price outlet stores. These retailers operate outlet stores as a separate distribution channel to sell their excess or damaged merchandise at discounted prices.[52] These off-price outlets include Saks Fifth Avenue's OFF 5th, Nordstrom Rack, and Bloomingdale's Outlet.[53] In addition to carrying merchandise from their respective full-price retail stores, these off-price outlet stores often also carry private label brands.

E. Boutiques

Boutiques, which are smaller retail stores (and may even occupy less than 2,000 square feet), target a specific niche market or sell unique products. Traditionally, the term "boutique" was used to describe an independent, "one-of-a-kind" brick-and-mortar store that specialized in fashionable apparel or accessories for a local market. More recently, the term "boutique" has been used to describe chains of smaller stores, such as Intermix and Scoop, which target fashion-forward women in their twenties and thirties,[54] and online retailers that offer unique products. Boutiques typically buy a limited amount of pieces from the collections of several different brands, and curate their merchandise to reflect their image or style. Boutiques operate on a smaller scale than department stores, appealing to customers seeking a more personalized shopping experience. At a boutique, a customer may have the ability to develop a relationship with the boutique's owners.[55]

F. Pop-Up Shops

Pop-up stores are temporary retail locations set up by brands or retailers to offer selected merchandise for sale for a limited time period. Pop-up stores are generally intended to raise brand awareness and to attract consumer interest rather than to generate significant revenues. The pop-up store concept has been used both by high-end and mainstream brands. High-end brands may gravitate towards temporary concept stores to reach a broader audience, even if visitors are only entering the store to browse, while mainstream brands may use pop-up stores to offer more limited and exclusive items. Online retailers often use pop-up stores as a test prior to opening a full brick-and-mortar store.

G. Internet Retailers

Although most brick-and-mortar retailers now have an online presence, there are some retailers that use the internet as their exclusive or primary retail sales channel. Some internet retailers, such as Amazon.com, offer a broad range of merchandise, while other internet retailers, such as BaubleBar (which sells fashionable jewelry at affordable prices), specialize in a single category of products.

In recent years, Amazon has grown to be the world's largest online retailer and one of the largest retailers of any kind in the United States.[56] Amazon has grown by expanding into a variety of merchandise categories and by acting as both a business-to-business service provider (including cloud computing services and third-party marketplaces), and as a retail sales channel. Amazon's success has significantly impacted the retail industry as traditional retailers are investing heavily to improve their online operations and in-store customer experience to more effectively compete with Amazon.

Online apparel retailers face certain marketing challenges that are not faced by brick-and-mortar retailers. Customers cannot physically feel the texture of the clothing or try on garments for proper size, styling, or fit. Accordingly, customers rely more heavily on visual images, detailed product specifications, and customer reviews located on the online retailers' website pages. Online retailers are increasingly providing customers with improved ways to view their products online, including by utilizing photographs from different angles, zooming features, and videos in which customers can see the apparel or accessories on models in movement. They are also offering consumers more personalized services, such as the "chat with a specialist" option available on many sites and are tracking consumer preferences more closely than traditional retail stores.[57] Many online retailers offer fast and free shipping options, and have more lenient return policies than brick-and-mortar retailers to compensate for the customers' inability to try on apparel and accessories before making purchases. Some brick-and-mortar retailers are able to offer rapid same-day fulfillment options by filling online orders from their brick-and-mortar retail stores (either through in-store pickup options or by delivery from the store). Online retailers are pursuing various strategies to offer comparable delivery options, including partnering with brick-and-mortar retailers and using distribution centers and third-party delivery services.

Online flash sale sites, such as Gilt, Rue La La, and Ideeli, have attracted a broad customer base. Gilt, the first of these flash sale sites, offered manufacturers an outlet for excess designer goods, but with a higher profile, fashionable image so the brands would not tarnish their high-end image by selling at deeply discounted prices.[58] Flash sale sites cater to urban sophisticates and largely gained popularity based on word of mouth marketing, building a loyal customer base.[59] By emphasizing limited supplies and a limited time to purchase the merchandise, Gilt prompted customers to make rapid purchasing decisions. Nearly 50% of the company's revenue was generated within one hour of a sale launching.[60] As more flash sale sites have emerged, and the quality and quantity of available merchandise has decreased, Gilt's growth has slowed. In response to competition from new flash sale sites, Gilt has undertaken a variety of initiatives to boost its growth, ranging from adding sales for luxury vacations and restaurants meals, to offering private-label brands manufactured in Los Angeles factories.[61]

Other new e-commerce business models have emerged, including personal subscription retail services, such as ShoeDazzle and JustFab; collaborative consumption online retailers, such as Rent the Runway and Bag Borrow or Steal; and retailers offering pre-owned or vintage fashion, such as The RealReal and ReFashioner. Personal subscription online retailers offer subscribers a selection of goods to purchase every month, based on style surveys, at a flat rate.[62] These personal subscription models may generate relatively steady revenue streams.[63] ShoeDazzle, which also benefits from endorsements and monthly style selections by celebrities, offers stylist-selected shoes at affordable prices.[64] Collaborative consumption online retailers, such as Rent the Runway, offer customers the ability to rent or "borrow" high-end and luxury merchandise, such as handbags and apparel, for a fraction of the full retail price for a limited time period. This business model assumes that certain luxury items may be used only for a single occasion, or reflect the current trend only for a single season, and therefore renting such items may be more attractive than paying the full purchase price to own them.[65] Retailers of pre-owned fashion often target specific market segments (such as high-end designers) and may emphasize the eco-friendly nature of reselling pre-owned fashion products. Online auction sites, such as eBay.com, facilitate online sales of both new and pre-owned apparel and accessories.

H. Mail-Order (Catalog) Retailers and Television Retailers

Mail-order (or catalog) retail and television retail represent a small portion of global retail sales, but are important retail distribution channels. Mail-order retailers (such as L.L. Bean, Inc.) historically did not invest in stores or traditional forms of advertising, but marketed their merchandise to targeted customers through catalogs, from which customers could place orders by mail or over the telephone. Mail-order retailers typically maintain highly valued lists of customers who have purchased merchandise in the past and monitor their customers' purchasing behavior.[66] Mail-order retailers are able to reach a broad consumer base without investing capital in opening brick-and-mortar stores. The rising costs of printing and mailing, combined with the growth of the Internet, however, have reduced the number of catalogs that are mailed annually to consumers from 17.2 billion in 2003 to 12.5 billion in 2011. Many mail order retailers now also offer online ordering options, and use web-based advertising and email messaging to supplement their printed catalogs.[67] In 2013, it was estimated that the mail-order industry will reach $835 billion in sales by 2015.[68]

Home shopping retailers, such as ShopNBC, HSNi, and QVC Inc., use television shopping channels to sell a broad range of merchandise, including apparel, accessories, and cosmetics, which customers order over the telephone or online.[69] Home shopping channels typically sell exclusive products through daily broadcasts with a broad customer reach. QVC reaches 100 million households in the United Stares, and in 2012 formed a joint venture for a home shopping channel in China.[70] Home shopping retailers may also have brick-and-mortar stores.

10.2 ARRANGEMENTS BETWEEN RETAILERS AND VENDORS

The line between fashion brands and fashion retailers is increasingly indistinct. Many fashion brands sell their products directly to consumers through owned or licensed retail stores, catalogs, and their own e-commerce platforms.[71] Through direct to consumer sales, a brand owner can offer its entire product line and create a "showcase" for the brand.[72] Many brand owners, however, continue to distribute their products by selling them at wholesale prices to retailers, such as department stores and Internet retailers, who in turn resell them at retail prices to the ultimate consumer. This strategy can significantly expand the geographic consumer base for the brand. A company may engage in either "open distribution," in which it sells its products to any type of retailer, or "selected distribution," in which it sells only to select retailers based on their geographic or customer profile.[73]

The arrangements that govern the relationship between the company, as vendor, and the retailer, as buyer, include a combination of standard terms and conditions, individual purchase orders, and oral agreements. The Model Uniform Commercial Code, which forms the basis of uniform commercial codes adopted in all fifty states,[74] provides a framework for interpreting the agreements between the vendor and the retailer, and also provides default rules for matters where the agreements are silent or unclear.[75] In particular, Article 2 of the Model Uniform Commercial Code, relating to sales, "applies to transactions in goods," but not services.[76] For the purposes of this section, all references to the "UCC" are to the Uniform Commercial Code as in effect in the State of New York.[77]

This section describes the principal elements of the arrangements between vendors and retailers.

A. Vendor Standards

When an apparel or accessory vendor and a retailer form a relationship, they typically agree to a set of terms and conditions that will govern purchases and sales between the parties. In many cases, the retailer (particularly a large retailer) possesses more of the leverage in this negotiation, as there are often numerous vendors competing for space in the stores (physical or virtual) of a limited pool of retailers.[78] Retailers prefer that vendors accept the retailer's terms and conditions because they tend to be both retailer-friendly in substance and comprehensive in the issues they address. Having standard terms and conditions that apply to all vendors with which the retailer does business also eases the administrative and operational burden on a retailer that manages relationships with numerous vendors.

A retailer often posts its extensive terms and conditions, sometimes called a "vendor standards" or "vendor compliance" manual, on a website for potential vendors to review. Vendors often can access these documents after logging into a secure site. The vendor standards cover the retailer's policies, procedures, and standards, including technology for transmitting orders, labels (including Universal Product Code, or "UPC" requirements), packing and presentation of products, audits, shipping (typically the vendor pays all freight and handling), routing, returns, terms of payment, and insurance. The vendor standards also include company policies regarding safety and sustainability, and compliance with labor standards. The retailer may also have supplemental vendor standards depending on the type of product. The vendor must sign a legal compliance form (a short document indicating it agrees to the vendor standards) as a prerequisite to a business relationship with the retailer.

Certain vendors, particularly luxury fashion brands that have more exclusive distribution strategies, may have the leverage to negotiate individual agreements with retailers that have different terms than the retailer's vendor standards. Similarly, a retailer may be willing to consider specific deviations from its vendor standards in order to maintain an important vendor relationship.

A vendor may request copies of the financial statements of a retailer or other assurances that the retailer can pay for the items that it orders. This is more common where the retailer is a small-volume specialty boutique rather than a large department store chain with publicly available financial statements. A vendor's factoring firm also may require certain credit checks of retailers before accepting invoices.

As part of the vendor standards, particularly for department stores, a vendor may agree to invest in electronic data interchange (EDI) technology systems that link the vendor and the retailer through interconnected computer terminals. The retailer uses electronic point of sale scanners to read the bar code on each product that is sold, and then relays information to the vendor as to the color, size, and sale price of such product.[79] This exchange of data allows vendors to tailor their production to more closely fit consumer demand. EDI also makes shipping and distribution more efficient.

Moreover, EDI enables retailers to maximize efficiency by automatic replenishment (the "just in time" reordering of certain merchandise) based on changing inventory levels and projected requirements. Automatic replenishment is most commonly used for basic items, which are easier and faster to produce than seasonal or fashion apparel, and are increasingly being manufactured in automated factories.[80] A stock keeping unit (SKU) is a unique identifier assigned to each product that a retailer sells. The retailer will perform a bulk projection for each SKU at the beginning of each season. Thereafter, based on sales data that the retailer generates and transmits to the vendor through EDI, additional products are automatically reordered as necessary, depending upon which sizes and colors the retailer sells to customers. The retailer might require special standards for vendors to participate in automatic replenishment, such as consistently being able to fill purchase orders at a certain percentage.[81] A recent study has indicated that when the relationship between retailers and their vendors is collaborative, such as sharing point of sale data, both parties can benefit.[82]

B. Selecting Products; Discounts and Markdown Allowances

Retailers may arrange for the purchase of products from vendors as many as six to nine months before the products will arrive in retail stores (though this lead time continues to shorten).[83] For major retailers, the retailer's management may set overall annual financial objectives for the retailer; thereafter, each of the retailer's buyers may develop a merchandise plan, consistent with these objectives, based on historic sales data and recent trends.[84] Buyers may go "to market" and meet with individual vendors in their showrooms to review the set of product samples in the vendor's line for each season. The vendors may give the retailers product catalogs or linesheets (documents that contain renderings of the styles (with size, color, and price information)) available for production, to aid them in placing their orders.[85]

New technology is impacting the market experience by allowing retailers and vendors to perform more transactions online. For example, Joor is an online global fashion marketplace for wholesale buying that connects fashion brands with retailers; brands can upload their linesheets and retail buyers can digitally browse and order merchandise.[86] In 2012, over $100 million in transactions were completed through Joor.[87]

A retailer may agree to purchase from a vendor specific quantities of particular SKUs, broken down by color and size. Because the products have not yet been produced, this agreement is tentative. Orders could be canceled by the vendor for a variety of reasons; for example, the vendor might not have received enough orders from its retail accounts to make production of a certain style or color cost-effective, or there could be a delay in production caused by circumstances outside of the vendor's control.[88] The retailer and the vendor typically will communicate throughout the production process in order to address any such issues in advance of delivery of the products.

Retailers rarely carry a vendor's complete line and, instead, choose styles that they expect to sell well, given their customer profiles. Retailers may also negotiate exclusivity arrangements, under which the vendor agrees not to sell certain SKUs to any other retailers. Often, a vendor and a retailer will negotiate a front-end discount (for example, 10% off the wholesale price of a vendor's product). The front-end discount is often only a verbal understanding, without written documentation; in some cases, it may be a long-standing arrangement that applies to all products sold by the vendor to the retailer.

Markdown allowances (MDAs) are a form of support that a vendor may provide to a retailer at the end of a season if the vendor's products fail to sell at the full retail price (and therefore must be discounted).[89] The rationale for MDAs is that vendors should be required to absorb part of the cost if their products do not sell well in the retail stores.[90] The retailer may also return to the vendor products that do not sell during the season and deduct a corresponding amount from the vendor's account.

The level of MDAs depends on the vendor's business strategy and industry standards. A vendor is often willing to pay MDAs to encourage a retailer to continue to buy its products. Similar to front-end discounts, MDAs are rarely documented in a written agreement and are typically a verbal understanding. This is consistent with UCC § 2-202, which provides that parties' written agreements may also be explained or supplemented by course of dealing, usage of trade, or course of performance.

The New York Supreme Court, in a 2007 decision, found that a course of performance between a vendor and a retailer could supplement the retailer's vendor standards manual.[91] Where performance takes place in repeated occurrences, acceptance of past practices is relevant in interpreting the parties' agreement. Thus, the court declined to dismiss the vendor's claim alleging improper markdown allowances, noting that:

> Where the contract for sale involves repeated occasions for performance by either party with knowledge of the nature of the performance and opportunity for objection to it by the other, *any course of performance accepted or acquiesced in without objection shall be relevant* to determine the meaning of the agreement.[92]

C. Purchase Orders

The UCC broadly defines the concept of a contract, providing that "a contract for the sale of goods may be made in any manner sufficient to show agreement, including offer and acceptance, [and] conduct by both parties which recognizes the existence of a contract . . . ."[93] As long as there is agreement between the parties, a contract may be found notwithstanding that it cannot be determined when the contract was made, or if specific terms are missing from the contract.[94]

The retailer's vendor standards may expressly specify that the transmission of the purchase order constitutes an offer.[95] The UCC provides that unless otherwise indicated, an offer may be accepted "in any manner and by any medium reasonable in the circumstances."[96] However, the vendor standards might specify that a vendor's acceptance may be indicated by written confirmation, shipment of goods, participation in an inventory replenishment program, or other performance consistent with acceptance.[97] The UCC provides that, between merchants, if an offeree includes additional or different terms in its acceptance, such additional or different terms would become part of the contract unless the offer expressly limits acceptance to the terms of the offer.[98] Therefore, vendor standards often provide that acceptance of the offer constitutes the vendor's acceptance of all terms and conditions therein, and that the retailer's prior written consent is required for any different or additional terms in the seller's acceptance.[99]

D. Shipping, Delivery and Risk of Loss

To facilitate the purchasing process, the retailer and the vendor need to agree on the shipping and delivery terms for the purchased products. For large retailers, a vendor may ship goods to the retailer's distribution center (DC). Items are then regrouped and shipped from a centralized DC to the retailer's individual stores. The retailer and the vendor must also agree on which party bears the cost and risk of loss for each part of the shipping and delivery process.

The International Chamber of Commerce developed a set of short-hand shipping and delivery terms called "International Commercial terms" or "Incoterms" to be used in international commerce (though the latest version of Incoterms recognizes the application of Incoterms to both international and domestic transactions).[100] Parties that wish to incorporate these standard shipping and delivery terms into their agreements must specify that the Incoterms definitions apply.[101]

In the absence of such specification, the relevant state law will apply. The Model Uniform Commercial Code historically contained a similar set of default shipping and delivery terms governing domestic transactions; these provisions, however, were repealed by the drafters due to concerns that they were "inconsistent with modern commercial practices." Presumably, the significant, but not exact, overlap with the Incoterms created confusion.[102] Under the current Model Uniform Commercial Code, shipping and delivery terms are interpreted in light of applicable usage of trade, course of performance, and course of dealings between the parties.[103] However, most states, including New York, have not amended their versions of the Uniform Commercial Code to eliminate the default shipping and delivery terms, and the definitions of those terms continue to govern domestic transactions in such states.[104]

Commonly used UCC shipping and delivery terms include the following:

- ***F.O.B. ("free on board")*** means that the risk passes from sender to receiver at the specified location.[105] Thus, for orders that are shipped "FOB DC," the vendor is responsible for delivering the goods to the DC, and the risk of loss of the goods does not pass to the retailer until the goods arrive at the DC. In contrast, if an order is shipped "FOB factory," title passes to the retailer and the retailer assumes responsibility when the goods are loaded onto the transport vehicle at the vendor's factory. Returned goods are generally shipped by the retailer "FOB origin," which means the retailer has a duty to ship the goods from the origin at the retailer's premises, not to deliver the goods to the vendor at its warehouse.[106] The risk of loss does not pass until the goods are loaded onboard the carrier at the origin.[107]
- ***F.A.S. (free alongside ship)*** means the risk passes from seller to buyer when the goods are brought alongside the vessel at a designated location.[108]
- ***C.F.*** or ***C. & F. (cost and freight)*** indicates which party bears the freight costs, when a different party bears the risk of loss. For example, if goods are shipped "C.F. DC," the vendor pays for the freight to the DC, but the risk of loss passes upon shipment at the vendor's warehouse.[109]
- ***C.I.F. (cost, insurance, and freight)*** is similar to C.F. except that the costs required to be borne also include insurance.[110]

E. Acceptance and Terms of Payment

Under the UCC, the buyer has a right to reject goods that do not conform to the parties' agreement.[111] In addition, under the UCC, the buyer has a right to inspect goods before payment or acceptance.[112] The UCC provides that goods are deemed to be accepted when, after a reasonable opportunity to inspect, the buyer accepts the goods, fails to reject the goods, or takes actions inconsistent with the seller's ownership of the goods.[113] Acceptance precludes the buyer's rejection of the goods.[114]

Once the goods are accepted, the retailer becomes obligated to pay the vendor. Where a contract requires payment before inspection of the goods, such payment does not impair the buyer's right to inspect the goods.[115] A retailer's vendor standards may further provide that the retailer reserves the right to hold for the vendor or return to the vendor any rejected merchandise.[116]

Because of the frequency of transactions, a vendor normally maintains an ongoing trial balance with the retailer, reflecting the numerous payments and adjustments between them. The vendor has a strong interest in receiving payment promptly, to increase its cash flow and maximize its ability to produce additional products.

F. Chargebacks

Although the retailer has a right to inspect the goods before they are deemed accepted, in practice it is logistically impossible for the retailer to inspect immediately the thousands of SKUs it receives. Many retailers provide in their vendor standards that acceptance of non-conforming goods is not a waiver of the retailer's right to recover damages.[117] Therefore, the retailer typically recovers damages after acceptance, in the form of "chargebacks."

Chargebacks are deductions from a vendor's account for any failures to comply with the vendor standards. Vendor standards typically specify that the vendor must ship in exact conformity with the purchase order.[118] The retailer will assess chargebacks if the vendor ships fewer units (a "shortage"), more units (an "overage"), or different units than as stated on the purchase order ("distortion"). Chargebacks are assessed at different rates depending on the type of noncompliance. For example, chargebacks may range from $25 per receipt, plus a per unit cost, for missing hangers, to $250 per receipt, plus a per carton cost and freight, for shipping to the wrong distribution center, to 100% of the purchase price plus all expenses incurred by the retailer for shipping prohibited furs.[119] These chargebacks are reflected in offsets against amounts payable by the retailer to the vendor. Occasionally, the retailer will choose not to deduct chargebacks owed for the sake of preserving a relationship with the vendor if, for example, it receives only a few damaged goods out of an otherwise acceptable shipment.

Deficiencies in product shipments are not always discovered immediately; often, they are not discovered until the retailer conducts its next periodic inventory, which can sometimes be up to a year later. Some retailers require or encourage their vendors to utilize radio frequency identification (RFID), a system that uses radio frequency electromagnetic fields to transmit information wirelessly and automatically identify a product that is labeled with such a tag.[120] This enables retailers to take inventory of their stock by waving a detector wand over multiple items rather than scanning each item's bar code individually.[121]

It is not uncommon for vendors to dispute chargebacks and other retailer deductions through legal action.[122] From the viewpoint of retailers, however, chargebacks create incentives for vendors to adhere to their agreements with retailers and allow retailers to process items more efficiently. One vendor standards manual states: "The purpose is not to chargeback your company, but to achieve compliance so we can move merchandise to the selling floor quickly."[123]

Retailers typically do not assess chargebacks on late or unfilled shipments, and instead the retailer has a right to cancel these orders. Recognizing that most apparel sold in the United States is manufactured abroad, the parties typically try to work together in the event of a delay in the supply chain.[124] However, late shipments may impair a vendor's eligibility to participate in an automatic replenishment program,[125] and repeated late shipments may cause the retailer to terminate its relationship with the vendor.

G. Consignments

Another form of contractual relationship between a vendor and a retailer is a consignment transaction, in which the retailer pays the vendor for the product *only after* the retailer has actually sold the product to the ultimate consumer. This arrangement shifts to the vendor the risk that products will not sell in the retail stores. The retailers can generate profits from any consigned products that are sold in its stores, without incurring any losses for unsold stock. Consignment arrangements permit retailers to carry and sell more products, resulting in a larger variety of merchandise for customers.

New or small vendors may agree to a consignment arrangement with a retailer for a trial period. If a vendor can demonstrate that its products have high sales volume, high margin, and "turn" (the ability to sell the entire quantity initially shipped to stores), then the retailer may be more likely to form a long-term relationship with the vendor.

10.3 DISTRIBUTION AGREEMENTS

Brands seeking to expand the sale of their products into new territories may use distributors to sell to retailers in such territories, rather than using their own sales personnel or independent sales agents. A distribution agreement is an agreement between a brand and a distributor pursuant to which the distributor purchases specified products from the brand at an agreed price and resells them to retailers in the territory covered by the agreement. Distributors typically resell the products at a higher price, but in some cases may take a percentage of sales as compensation. In a typical distribution arrangement, the distributor holds inventory in the territory, undertakes marketing and promotion in the territory, performs after-sales service, and takes the credit risk for sales of the products in the territory. A distribution agreement can be a cost-effective way for a brand to develop a consumer base for its products in a territory where it previously had only a minimal presence.

There are, however, disadvantages to using distributors. The distributor, rather than the brand, will have control over the marketing and sales process; accordingly, inappropriate conduct by the distributor could negatively impact the image of the brand. In addition, the amount of the distributor's mark-up may make the products less competitive with comparable brands sold directly by the manufacturer in the territory. Furthermore, the brand will not have a direct relationship with the retailers of its product, which may impair the ability of the brand to move to direct sales in the territory in the future.

NOTES TO CHAPTER 10

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