

A Report on the Status of the Relationship Between Operators and Bottlers

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I) Introduction

The NAMA Business Plan for the period from 1999 to 2002 required the association “to serve as a catalyst to facilitate conversation and improve relationships between bottlers and operators.” In fact, of the 24 goals laid out in the 3 year Plan, improving relations between bottlers and operators was listed number one. In furtherance of that goal, the NAMA legal staff issued a report in May of 2002 which examined the problems that existed between soft drink bottlers and vending operators, recounted the steps NAMA had taken over the three year period to improve the relationship between these two critical segments of the industry and suggested additional steps that the members or NAMA might undertake to improve the relationship. The report was sent to the NAMA Board of Directors in advance of the June, 2002 Board meeting and was discussed at that meeting.

Since then, the NAMA Board of Directors has approved a Business Plan for the years 2003 to 2005. This new plan, following the priorities of the earlier Plan, emphasizes the importance of the operator-bottler issue by addressing the matter in Section 1A of the Plan:

NAMA shall “facilitate better understanding and improved relations between vending operators and soft drink bottlers, focusing on the overriding issue of fair play and a level playing field.” Further, the 2003-2005 Plan requires NAMA to communicate the Operator-Bottler Report to the members.

But first, it is important to emphasize that NAMA is a vertically integrated association serving the food and refreshment vending industry. That is, it includes in its membership operator companies that sell food and beverage product through vending machines to the public, as well as product suppliers, including bottlers of soft drinks and finally, product and equipment manufacturers. Among the manufacturers of product are the major soft drink syrup manufacturers---Coca-Cola, Pepsi Cola and Dr. Pepper/Seven-Up. As of December 31st, 2001, NAMA had in its membership 1542 Operator Members, 337 branches of operators, and 401 product suppliers. Although 61 operator members checked the box “bottling operations” on their 2001 dues renewal notice, it is obvious that a great many did so in error. We believe that only 10 of these 61 operator members are actually engaged in bottling operations.

The NAMA Board of Directors includes a representative of the Coca-Cola Company and, until recently, a representative of the Pepsi Cola Company. There is no representative of a soft drink bottling company currently on the Board of Directors. Now to the sometimes contentious relationship between vending operator and soft drink bottler:

II) What is the Problem?

A. Soft Drinks Dominate the Vending Market

The first component of the problematic relationship between operator and bottler is that soft drinks dominate the vending market. According to one trade journal, soft drinks accounted for 29.9% of vending machine sales in 1974 in dollar volume. This percentage grew to 41.6% by 1985 and by 2001, 55.3% of the industry’s sales were in soft drinks. (This figure of 55.3% includes bottled cold drinks, canned cold drinks, cup cold drinks and 1.8% of gross sales in juice products sold through dedicated juice machines.)

During this same 27-year period, according to the same trade journal, the industry grew from \$8.8 billion in sales to \$38.7 billion. In contrast to the explosion in vended cold drink sales, hot drink sales, which stood at 7.5% of industry sales in 1974, increased to only 9.3% of sales in 2001. (It should be noted there was a noticeable and encouraging increase in hot drink sales between 1999 and 2001----up from 8.0% of gross sales to 9.3% of gross sales.) Cigarettes accounted for an astounding 30% of vended sales in 1974 and plummeted to 2.3% of sales in 2001. Based on these raw figures, it is clear that any nascent problems that existed between vending operators and soft drink bottlers in the 1970's would be greatly magnified as the industry moved toward more dependence on cold drink sales through the 1980's and '90's.

Within the vended cold drink market, there was a shift away from cup drinks, with more emphasis on canned and bottled sales. Between 1974 and 2000, cold cup drink sales as a percent of gross vending sales declined from 7.5% to 5.2%. This decline took place in spite of data showing that cold cup machines consistently outperformed their can machine competitors. For example, the NAMA Operating Ratio Report for 1994 put average annual sales per can and bottle machine at \$4,814 with a gross profit margin of 55.5%; equivalent figures for the cold cup vending machine were \$5,385 and a 71.7% gross profit margin. NAMA's Operating Ratio Report for 2001 shows gross sales per can machine of \$3,831 and a gross profit margin of 52.8%; gross sales per bottle machine were reported at \$5,168 with a gross profit margin of 49.1%. Again, cold cup machines excelled, with gross annual sales per machine of \$5,514 and a gross profit margin of 62.6%. Larger companies, with sales over \$10 million, did even better, with a gross profit margin on cold cup sales of 64.6%.

In telephone conversations during the fall of 2001, operator members offered several reasons for this shift away from cup vending: one was the high cost of cup equipment vs. can and bottle equipment. Another was the cost of labor---- maintaining cup equipment is far more labor intensive than maintaining can and bottle equipment. Lastly, a number of operator members stated that customers prefer the can or bottled drink to the cup drink. Customers, these operator members said, believe the quality is better in the case of the prepackaged soft drink. But one operator member pointed out that virtually no fast food outlet in America offers its customers can or bottled soft drinks----only cup drinks.

In light of these facts, vending operators would do well to take another look at cold drink cup vending. The increased investment in equipment and labor might, over the long haul, yield higher profits for the vending company. Further, increasing cup vending could reduce the operator's dependence on his traditional bottler/supplier. Our research indicates that conditions exist for more price competition in the syrup market than in the can and bottle market.

This quote is taken from The Coca-Cola Company's Form 10-K filing with the Securities and Exchange Commission of March, 2000:

“Under the terms of the Bottlers' Agreements, bottlers in the United States are authorized to manufacture and distribute Company Trademark Beverages in bottles and cans, but generally are not authorized to manufacture fountain syrups. Rather, the Company manufactures and sells fountain syrups to approximately 589 authorized fountain wholesalers (including certain authorized bottlers) and some fountain retailers. The wholesalers in turn sell the syrups or deliver them on the Company's behalf to restaurants and other retailers. The wholesaler typically acts pursuant to a non-exclusive letter of appointment which neither restricts the pricing of fountain syrups by the Company nor the territory in which the wholesaler may resell in the United States.” The significance of this non-exclusivity feature of the syrup market will become more apparent when we treat the bottlers' exclusive territories in the can and bottle market.

B. Price

The second element of the often times heated relationship between vending operators and soft drink bottlers, and the one most frequently cited by operators, is price. Quite simply, many operator members don't think they get a fair price from their bottler/supplier. "I have to pay \$7 or \$8 a case for soft drinks, and I buy by the trailer-load. I go to the grocery store and see the same case of drinks selling for \$4 or \$5." This complaint, made by a vending operator from the south, is typical of complaints heard from operators coast-to-coast for many years.

Separating cold facts from heated claims about prices is difficult. But the printed word is usually more reliable than the spoken. In July 2000, a Midwest operator filed a written complaint with the Attorney General of Iowa about prices for soft drinks. The vendor said that grocery store soft drink prices to consumers were lower than the wholesale prices the vendor was paying to his bottler-supplier. Here's Pepsi-Cola General Bottler's written response of August 14th, 2000: "(The vendor) complains that grocery store retail pricing to consumers is lower than the wholesale price charged to third party vendors. Several points need to be made on this issue. First, many grocery chains sell carbonated soft drinks at a loss to bring customers to their store. This practice means that the retail price is often lower than what the grocers are charged. Second, while the retail pricing identified (by the vendor) does not include the \$1.20 per case deposit, the \$8.00 price does. Accordingly, to compare apples with apples, the third party vendor price we should be focused on is \$6.80, not \$8.00. Third, the price difference between \$6.28 and \$6.80 on a 24-can case is nominal and largely a factor of the higher volumes (as most pricing is) sold by the grocery channel. Finally, it bears noting that vendor pricing on 20 ounce non-returnable bottles, the fastest growing segment of the market, is lower than our pricing for the grocery channel. Again, this is largely because vendors sell a greater volume in this size than grocers."

Whether the 2 cent-per-can price difference is nominal is arguable, but what is not arguable is that higher volume justifies lower price. A typical supermarket sells more soft drinks than a typical vendor. And, because a supermarket sells thousands of items, it can afford to use soft drinks, from time to time, as a loss leader. A great many vendors, in contrast, sell essentially the same items they sold 30 years ago---snacks, candy and cold drinks. (Of course, cigarettes are the exception.) Unlike the supermarket, the vendor must always make a profit on his soft drinks.

And, there are other means available to the supermarket but not available to the vendor that increases the supermarket's volume and thus its price advantage over the vendor. Advertising stands out. A case before the Federal Trade Commission in 1994 involving a major bottling company gives a good idea of the power of advertising: the Commission found that an "ad feature" run by a supermarket in a local newspaper advertising low prices for soft drinks could give the bottler up to ten times the non "ad feature" volume. It's no wonder the bottler gives an attractive price to the supermarket. The vendor has no similar advertising opportunity.

And while the supermarket offers a wide variety of soft drinks, the vending channel is more limited. This statement is taken from the same 1994 Federal Trade Commission opinion in which the soft drink bottler, Coca-Cola Co. of the Southwest, was ordered to divest itself of a Dr. Pepper/Seven Up franchise:

“In addition, the evidence shows that carbonated soft drinks sold in vending machines are almost entirely brands that are direct-store-door delivered, not warehouse or private label brands. Vending machines are stocked with nationally branded carbonated soft drinks, with virtually no private label brands available. Moreover, although private label brands may be marginally more available in the fountain channel, since a few restaurant chains sell certain flavors as their own private label brand, the record does not establish that the occasional presence of non-branded carbonated soft drinks in the cold drink channel would provide a constraint on the pricing of branded carbonated soft drinks.”

Telephone conversations in the fall of 2001 and the winter of 2002 with vending operators confirmed that little has changed in the soft drink vending market since 1994. “The soft drink vending market is still pretty much a Coke and Pepsi market,” said one vendor. Thus, the lack of a substantial alternative to the two major branded carbonated soft drinks in the vending channel exacerbates the vending operator’s pricing difficulties.

However, there is one factor regarding price that should weigh in favor of the vending operator but oftentimes appears not to be reflected in the price he pays: the cost of delivery. “Delivery to the vendor is the cheapest in the retail industry. The bottler just backs up a truck to my warehouse,” said one vendor. In contrast, delivery of product to the supermarket is generally “door-to-store” delivery. This means the product is delivered directly to the retailer’s store and the *bottler’s* employee arranges the product on the store’s shelves, removes old product, faces the products’ label toward the customer, and ensures that merchandising and advertising signs are properly positioned. This would seem to be a more expensive delivery than in the case of delivery to the vendor.

One device available to vendors that might ease their soft drink price difficulties is the buying cooperative. A number of operators are members of buying cooperatives in which the power of volume purchasing is achieved through an alliance of vending operators. Savings are usually passed on to the vendor in the form of a quarterly or semi-annual rebate check based on the volume of product purchased. However, the buying cooperative can only be effective if bottlers participate. We will discuss in later sections of this report other steps operator members might take to address the pricing issue.

C. “I Have to Buy From My Competitor”

The third element we have identified in the rocky relationship between operator and bottler is that the operator must buy his canned and bottled soft drinks from his bottler/supplier who also owns and operates soft drink vending machines in the same market the operator is doing business in. It bears repeating that can and bottle soft drink sales comprise some 30 to 50% of many vending operators’ sales.

Soft drink bottlers, principally product finishers and wholesalers, don't own grocery stores, discount stores, C-stores or drug stores. But they do own and service vending machines. And, in recent years, there is evidence of soft drink bottlers moving more aggressively into the retail vending of soft drinks. An article in the New York Times in November, 1999, quoted John R. Alm, Chief Operating Officer of Coca-Cola Enterprises, the world's largest soft drink bottling company: "...earnings improvement is expected to come from more purchases made in the highly profitable 'cold drink' segment of the soft drink market, which includes vending machines. For the year, sales in supermarkets have fallen 6%, while cold drink sales have risen at a double-digit rate."

Two years later, Coca-Cola Enterprises' November 1st, 2001, Form 10(Q) filed with the Securities and Exchange Commission showed plans for continued movement into the soft drink vending business:

"The Company (CCE) participates in programs with the Coca-Cola Company, implemented under the master bottler contract between the Company and the Coca-Cola Company, designed to accelerate the placement of cold drink equipment in certain territories. Under these programs, the company receives reimbursements from the Coca-Cola Company of a portion of the cost of developing the infrastructure (consisting primarily of people and systems) necessary to support the accelerated placements. These reimbursements are recognized as an offset to expenses as incurred in the period for which the reimbursements are designated. Under the programs, the Company agrees to: (1) purchase specified numbers of venders/coolers or cold drink equipment each year through 2008, (2) place the equipment in specified territories of the Company, (3) maintain and stock the equipment in accordance with specified standards, and (4) report to the Coca-Cola Company minimum average annual sales volumes throughout the economic life of the equipment. Should the Company not satisfy these or other provisions of the program, the agreement provides for the parties to meet to work out mutually agreeable solutions.... No refunds have ever been paid under this program, and the Company believes the probability of a partial refund of amounts previously paid under the program is remote."

III) Equipment

The issue of competition between bottler and operator oftentimes involves the matter of equipment. According to one Coca-Cola official, "the whole problem began when vendors accepted free equipment from bottlers and signed agreements to stock only the bottler's product and then reneged on the contract." It has been common in the industry for a bottler to provide "free" equipment to a third party vendor in exchange for a promise to stock the equipment with only the bottler's product. But then along comes the client who requests that both major branded products be offered to his employees. The employees want choice. The vendor then accedes to the request; the bottler discovers the breach of contract and takes over the soft drink sales at the account.

Vending operators would do well to purchase their own equipment. We have noticed in our examination of the operator/bottler relationship that vendors who own their own equipment generally have a better relationship with their bottler than vendors who do not own their own equipment. The vendor who owns his vending machines can avoid agreements that restrict the beverages he can sell. Accepting "free" equipment often results in serving two masters-----the client and the bottler. This usually doesn't work. We did encounter one vendor who had a good relationship with his bottlers and he claimed that about 70% of his equipment was "free".

Before we move on to the law and the role it plays in the competition between operator and bottler, let's summarize the factors we've thus far identified that contribute to the problematic relationship between vending machine operators and bottlers: the problem appears to be the result of the industry's heavy concentration in branded carbonated soft drinks, the movement away from cup vending, the higher prices that vendors pay for can and bottle product, reliance on so-called "free" equipment, and competition in the vending channel from bottlers.

Now let's take a look at why vendors must purchase their product from their soft drink supplier-competitor.

IV) The Soft Drink Interbrand Competition Act

A. Background, Text and Commentary

From the earliest days of the soft drink industry, soft drink bottling companies were granted exclusive territories in which to bottle and sell their product. Parent soft drink companies, manufacturers of the patented syrup, thought it would be too expensive to ship the heavy finished product all over the country. A distribution system in which local, independent companies would buy the syrup, mix it with carbonated water and sell the finished product to retailers within a relatively small area made sense. The product was sold in returnable, refillable bottles. In the early 20th century, the exclusive territories were determined by how far a horse and wagon could go out with finished product in the morning and return in the afternoon with empty bottles. Independent bottlers with exclusive territories remained the model in the soft drink industry into the 1970's. But then the Federal Trade Commission ruled that the industry's exclusive- territory contracts with the bottlers were anti-competitive and illegal.

The soft drink industry responded with the Soft Drink Interbrand Competition Act. (hereafter referred to as the Act or the Soft Drink Act.) The Act passed the Senate 89 to 3 and the House by a vote of 377 to 34 in the summer of 1980 and was signed into law by President Jimmy Carter on July 10th, 1980. The Act passed by these wide margins in spite of the opposition of the Justice Department, the National Association of Attorneys General, foodservice trade groups (not including NAMA), and the Consumer Federation of America.

In the critics' view, the Act creates an unwarranted exception to the nation's anti-trust laws for the soft drink industry. The Act's supporters argue that it only clarifies anti-trust law, which was never intended to promote intrabrand competition, but only interbrand competition.

The Act states, in relevant part:

"Nothing contained in any antitrust law shall render unlawful the inclusion and enforcement in any trademark licensing contract or agreement, pursuant to which the licensee engages in the manufacture, distribution and sale of a trademarked soft drink product, of provisions granting the licensee the sole and exclusive right to manufacture, distribute, and sell such product in a defined geographic area or limiting the licensee, directly or indirectly, to the manufacture, distribution and sale of such product only for ultimate resale to consumers within a defined geographic area: Provided, That such product is in substantial and effective competition with other products of the same general class in the relevant market or markets."

In an interesting commentary on the Act appearing in the William and Mary Law Review in 1993, (Public Choice, Public Interest, and the Soft Drink Interbrand Competition Act: Time to Derail the Root Beer Express?) Professor Allan W. Vestal argues forcefully that the Act should be repealed.

The soft drink industry, Professor Vestal asserts, advanced two major arguments in support of the Act when it was under consideration in Congress in 1979 and 1980: that the Act would protect the environment by continuing the system of returnable bottles; and that it would preserve thousands of small, independently owned bottling companies in America. The Act would be good for the environment and good for small business.

Neither purpose, Professor Vestal argues, has been served by the Act. The refillable bottle, which had a 100% lock on the market in 1958, was already in serious decline by 1980, dropping to only 38% of the market by that year. Between 1980 and 1993, the use of refillable bottles declined by three-quarters. Today, there are virtually no refillable bottles for sale in America. And the Act, according to Professor Vestal, did not preserve the small, independent bottler in America. In the 1950's there were 6,000 bottlers in the United States. By 1970, the number of bottlers had declined to about 3,000. Passage of the Soft Drink Interbrand Competition Act in 1980 did not reverse or even halt this trend. By 1988, the number of bottlers had shrunk to about 1,000.

Not only was there a reduction in the number of bottlers in the United States, but the ownership patterns also changed. Large conglomerates such as General Cinema and Warner Communication bought bottling companies and both Coca-Cola and Pepsi Cola purchased a controlling interest in a number of formerly independent bottling companies.

Consolidation in the soft drink industry appears to have accelerated in the 1990's. According to the Coca-Cola Company's Form 10(k) filing with the Securities and Exchange Commission in March of 2000, "Approximately 59% of the Company's U. S. gallon sales for 1999 was attributable to sales of beverage concentrates and syrups to approximately 89 authorized bottler ownership groups in approximately 397 licensed territories. Those bottlers prepare and sell finished beverages bearing the Company's trademarks for the food store and vending machine distribution channels and for other distribution channels supplying home and immediate consumption. Approximately 33% of 1999 U. S. gallon sales was attributable to fountain syrups sold to fountain retailers and to approximately 589 authorized fountain wholesalers, some of whom are authorized bottlers.Coca-Cola Enterprises Inc. and its bottling subsidiaries and divisions accounted for approximately 48% of the Company's U. S. gallon sales in 1999. At February 15th, 2000, the Company held an ownership interest of approximately 40% in Coca-Cola Enterprises, which is the world's largest bottler of Company Trademark Beverages."

Regardless of whether the Act was wise public policy at the time of enactment, or whether, since then, it has accomplished its purported goals, the fact remains that the Act is still today a part of the nation's anti-trust law. Thus, if the bottler enforces his exclusive-territory contract, the vendor *must* purchase that brand's product from the sole supplier in the territory, or not at all. The vendor cannot shop around.

B. Transshipping: Some Do, Most Don't

At this point, a brief note about transshipping is called for. Transshipping involves a vendor purchasing his soft drink product from a bottler outside the bottler's territory in which the vendor does business. If discovered, the intruding bottler, not the vendor, faces very stiff fines. Our conversations with vending operators over the past 6 months suggest that most vendors buy their product from their local bottler. In other words, they do not transship. "Don't transship. If you do, your bottler will compete with you." That was the admonition of one operator.

We spoke with a few operators who said they transshipped, one of whom said he did it "because the local bottler didn't mind." Another vendor told us that one bottler policed the territory quite effectively, while the other brand's bottler hardly at all.

One vending machine operator claimed that an exception to the anti-transshipping convention has grown up over the years and that the exception rests on the distinction between “transshipped product” and “foreign product”. The distinction is best understood with a hypothetical: Vending Co. X, with headquarters and accounts in Illinois, also has branches and accounts in Iowa and Wisconsin. Each of the three markets is served by a different bottler of soft drink Brand A. Vendor X, according to this operator, can buy all his product from Illinois soft drink bottler A and “move it within his system”, selling it in his vending machines in all three states. According to this operator, the product he sells in Iowa and Wisconsin is permissible “foreign product”, not forbidden “transshipped product”. We cannot attest to the legitimacy of this practice; and, we simply do not know how widespread the practice is in the marketplace.

C. Two Observations

We are not experts in anti-trust law. Nor do we know everything there is to know about the Soft Drink Interbrand Competition Act. But having said that, we offer two observations about the Act before moving on to litigation interpreting the Act:

1) It is clear that Congress intended the Act, an Act that some would argue is an exception to the pro-competitive anti-trust laws and thus a provision of law that should be very narrowly construed, to legalize the protection contained in decades old exclusive territory contracts against incursions by same-brand bottlers in *the bottling and wholesaling* of soft drinks. It is at least arguable that Congress might not have intended the Act to give a bottler the clear price advantage he enjoys over his third party vendor/ competitor in the *retailing* of soft drink product through vending machines.

2) A great many vendors claim that among all the kinds of retailers that bottlers sell to – convenience stores, drug stores, supermarkets and others – the vendors, the only retailers with whom the bottlers compete, are charged the highest price for product.

V) Litigation

The Soft Drink Interbrand Competition Act has been the subject of litigation. Most of the litigation occurred from the late 1980's into the mid-1990's. We have read some of the case law interpreting the Act, but not all. Based on what we have read, from the point of view of those challenging the bottlers' practices, the litigation has been expensive and unrewarding. Typically, the litigation has focused on the condition bottlers have placed on their retailer/customer to resell only to consumers. The courts have consistently ruled in favor of the bottler, upholding his right, protected under the Soft Drink Interbrand Competition Act, to prevent transshipping by instructing his retailer/customer not to sell to resellers. This is why many vending operators have been turned down at the discount store when they have tried to buy soft drinks in bulk.

However, we note that in one case, *Owens v. Pepsi Cola Bottling Co. of Hickory, North Carolina*, (1993), the North Carolina Supreme Court emphasized that its holding, in favor of the bottler and his resale restrictions on convenience store owner Owens, was limited. The Court wrote: “The Soft Drink Act authorizes bottlers to impose wholesaling restrictions on their customers *only* to prevent transshipping. (Emphasis supplied by the Court.) Wholesaling restrictions imposed for any other purpose are outside the purview of the Soft Drink Act and are therefore subject to the full scrutiny of North Carolina law.”

We wonder how a court would rule where the evidence showed that the purpose and the effect of the bottler's prohibiting his retail customer from selling to a third party vendor (all of whose accounts were in the bottler's territory) was to permit the bottler to acquire more of the retail vending machine soft drink business.

One case involving a vending operator competing with a bottler in the soft drink vending market is Sun Dun v. Mid-Atlantic Coca-Cola Bottling Company of Washington D.C, et al (1991). Sun Dun, among other things, claimed that the price Mid-Atlantic charged Sun Dun was so high that it amounted to a refusal to deal with Sun Dun. The Court granted Mid Atlantic's motion for summary judgment on this allegation, noting that Mid-Atlantic charged Sun Dun the same price it charged ARA, Service America, Canteen and other vending companies competing with Sun Dun. But the court denied Mid-Atlantic's motion for summary judgment on Sun Dun's claim of unfair competition under Maryland law. Presumably, although this is not entirely clear in reports of this case, the unfair competition allegation was that Mid-Atlantic enjoyed a substantial and unfair cost advantage over Sun Dun in the soft drink vending market. But, as in other litigation under the Soft Drink Act, this issue never went to trial. Apparently, it was settled.

VI) Meetings and Presentations

In an effort to improve relations between operators and bottlers NAMA has convened or sponsored a great many meetings and presentations over the past 6 or 7 years covering the vendor/bottler relationship. For example, Jeff Schenk, a former Pepsi-Cola employee and later a consultant to the beverage industry has made several presentations to operator members at NAMA general membership programs, one state council officer meeting, and several individual state council meetings. His presentations have focused on educating operator members about the soft drink industry: its size, competitive factors, consumer preferences in taste, caloric content, packaging and the like. His message is that the more the vendor knows about the bottler, the better will he be able to work *with* the bottler to sell more products and make more money.

The Anti-trust laws and the restraints they impose on trade associations such as NAMA were discussed by Terry Hutton, an attorney with the firm of Howe and Hutton in Chicago, at a meeting of NAMA's state council officers in 1998; and Richard Reed, an attorney with the Federal Trade Commission, made a presentation on the anti-trust laws, the Soft Drink Interbrand Competition Act and litigation interpreting the Act at the NAMA state council officers' meeting in New Orleans in October, 2000.

Reed expressed the view that so long as the Soft Drink Act remained in effect, there was little the Courts could do to remedy what the operators perceived to be a playing field sharply tilted in favor of the bottler. Both attorneys pointed out the benefits that operator members could realize by joining buying cooperatives. And Richard Reed noted that operator members were free to write to their representatives in Washington urging repeal of the Soft Drink Act. He also recommended to operators that they stress service over price.

A meeting not convened by NAMA was held at McCormick Place during the NAMA convention in Chicago in October, 1998 for the purpose of determining the level of interest among operators in retaining counsel to research the industry and the law regarding the soft drink industry's practices vis-à-vis third party vendors. No NAMA employees attended this meeting but an attorney with the firm of Howe and Hutton attended the meeting as a representative of NAMA. It appears that nothing decisive came out of the meeting.

In the case of most industry meetings, representatives of the bottling companies, though invited, have not attended. Many meetings, particularly at the state council level, have deteriorated into fruitless "bottler bashing" sessions.

Regarding future meetings, we would offer this suggestion: NAMA should explore the idea of a panel-program featuring experienced vendors with solid relationships with their bottler. These vendors could tell the audience how they built these relationships. There is plenty to talk about in the soft drink vending business without getting into prices. The centerpiece might be the superior service that vendors unanimously claim over their bottler-competitors. With a series of well-thought-out questions and careful moderating, the program could produce 60 to 90 minutes of useful lessons from people experienced in the field.

VII) The School Market

“If they want it, they can get it.” Thus have many vending operators described the marketing programs of soft drink bottlers to win exclusive contracts to sell their soft drink product at the nation’s colleges, universities and high schools. Vending machine operators simply cannot match the generous fees, commissions and facility donations----the high school football or basketball scoreboard is the most notable example---that bottlers provide the schools. Establishing a soft drink habit and brand loyalty with young people is certainly the motive behind these bottler programs. We would guess that the bottlers, in defense of this marketing, would point out that as these customer-students graduate and become customer-workers in the nation’s factories and offices, they become the regular customers of the third party vendor.

We find nothing in federal or state law that would prohibit these exclusive contracts. But we do note the sharp reaction of state and local public officials in the past year to what they perceive to be excessive commercialism in the nation’s schools. And, we are well aware of the increasing focus on obesity in America and the resulting attacks on soft drinks and vending, particularly in schools. But that issue is beyond the bounds of this report.

VIII) People and Attitude

One experienced vendor explained that the solution to all the problems between the bottlers and operators is people with the right attitude. “Don’t approach your bottler in a confrontational manner. Sit down with him and say ‘we’re both in the soft drink business. How can we work together to sell more soft drinks and make more money?’ He continued: “Emphasize that vending is the perfect venue to test a new product and introduce it to the public. Explain to the bottler how you can service the machines better than he can. Tell him that you, the operator, can help him sell more product, but only if he gives you a fair price.”

IX) Summary and Observations

In examining the relationship between operators and bottlers, we have seen the major factors contributing to the problem that marks the relationship: the dominance of soft drinks in the vending industry, the movement away from cup vending, the higher prices operators pay for can and bottle soft drinks, some of the reasons for these higher prices and the competitive factor. We have also seen evidence that the bottling companies see vending as a profitable, growth market.

We have looked at the Soft Drink Interbrand Competition Act and the role it plays in the operator-bottler relationship and the arguments that were offered to Congress in 1980 to justify enactment of the Act. We have seen that litigation has not been helpful to the operator: the courts have ruled in favor of the bottler regarding resale restrictions and operator claims of unfair competition under state laws have generally been settled.

We have noted NAMA's efforts in holding meetings and presentations by experts in business and law. In the case of meetings, the objective has been to bring the parties together to discuss problems and arrive at solutions. In the case of presentations, the purpose has been to educate members regarding the bottling industry and inform them of the relevant laws that pertain to the marketplace.

We have made suggestions: among them, that operators not retreat from, but return to cold cup vending; that vendors join buying cooperatives; that, where possible, vendors purchase their own equipment, and that vendors work with their bottlers in a non-confrontational manner to sell more product and serve the customer better. Vendors should stress service.

We close with this observation: We are troubled by the apparent role that the Soft Drink Interbrand Competition Act is serving in propelling bottlers into the retail vending market. It is certainly clear that Congress intended the Act to legalize exclusive territory contracts in the bottling and wholesaling of soft drink product. But whether it intended the Act to bless the bottler with a clear advantage in the retail vending market is open to question.

NAMA will continue to work with soft drink companies, bottling companies and operator members to improve the relationships between these segments of the industry for the benefit of these companies and, in particular, the industry's customers.

More concretely, and in accordance with the 2003-2005 Business Plan, NAMA shall:

- 1) "Create a joint advisory task force with representatives on both sides of the issue to advise NAMA on how better to proceed."
- 2) "Complete a 'case for cooperation' position paper, which will include statements from operator members who have developed good relations with their soft drink suppliers."
- 3) Continue to encourage soft drink bottlers to join and become active with NAMA and the state councils.

Thomas E. McMahon
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