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# TESTIMONY

BY

DAVID R. JONES

BEFORE

THE
ASSEMBLY COMMITTEE
ON
COMMERCE AND LABOR

MAY 14, 2003

ASSEMBLY COMMERCE & LABOR 1 of 8
DATE: 5/14/03 ROOM: 4100 EXHIBIT E
SUBMITTED BY: David Jones

My name is Dave Jones. First I want to thank you, Chairman Goldwater, and members of the committee for holding this hearing and giving me an opportunity to address this proposed legislation. I have been in the retail business for twenty-three years and have dealt with tobacco companies for most of that time. Today I speak to you as a representative of PJ'S LIQUOR & WINE SHOP; a Nevada based Sub Chapter S-Corporation located in Gardnerville, Nevada. The business employs seven full time employees and last year had sales of 2.3 million.

Let me begin by giving you a brief verbal picture of the current nature of retail tobacco sales. There are basically two types of retailers. Those who aggressively seek to sell a volume of product by discounting, promoting, and carrying a very large selection of brands and styles. These stores sell about ninety percent of the total volume of tobacco. And the second group, those who do not discount, only carry a limited selection, and do not rely on the revenue of tobacco sales to keep their businesses viable. This group generally consists of supermarkets, drug stores and small rural stores. They sell only about seven percent of the total volume of retail tobacco. I will speak more of this group in later comments.

At PJ'S LIQUOR & WINE SHOP, along with our liquor sales we are an aggressive outlet for tobacco. We are a mid to large account, with sales in excess of five hundred cartons of cigarettes a week. To maintain this volume and stay competitive we must do several things:

- We must discount our prices. With few exceptions we work on a low profit margin of two to eight percent. The fierce competition among volume retailers guarantees a low retail price for consumers.
- We must carry a large and very costly inventory with an ever increasing number of brands and styles. Every customer is important to us. We will carry any brand or style they desire.
- We must contract with as many tobacco companies as possible.

Why must we contract? Answer: To participate in the tobacco companies "buy-down" and promotions programs. In a "buy-down" situation the tobacco company reimburses us a set amount, usually between six and nine dollars per carton, if we reduce our retail the same amount. Our competition does this and we must do the same. Promotions are generally a multi pack offering with free goods. An example would be "buy two packs get one free". Consumers know when these are available and expect that we will have them. Remember, only contracted stores participate in "buy downs" and promotions. A retail price six to nine dollars higher than the store down the street would mean the loss of your customers and your business. Contracting is not really a matter of our choosing, it is a necessity for survival.

The contract we must sign is the subject of this legislation. To contract with Phillip Morris we must give them fifty two percent of all the visible space we allocate to tobacco products. Don't be misled when they tell you they have many levels of contracts, they all require the same percentage of space. To contract with RJ Reynolds, the second largest company, we agree to give them thirty five percent of all visible space. In addition to the space issue we must agree to carry all brands and styles they dictate, whether they sell or not. We have to accept every new item they produce and we are obligated to accept additional inventory when they choose to send it. We have to wait, sometimes for months, for reimbursement of monies owed to us for promotions. These contracts are preprinted, no give and take, there is no negotiation, no meeting of the minds. You take it or leave it. With one-third or more of total sales coming from tobacco we must take it.

In our store these two companies control eighty-seven percent of the space visible to the consumer. They have more room than they need to merchandise their products and attract the eyes of the interested shopper. There is more than enough room to attach signage and promotional pricing. It is an example of overkill. The benefit to them is obvious; all of the competition is crammed into the remaining space or under the counter where no one sees it. Signage for these companies has to be very small so as not to cover another product. The consumer will most likely not even see it.

The only way to promote a product from one of the smaller companies is to put it on the counter. Of course, on the counter means it is self serve and Phillip Morris will penalize me ten cents a carton for every carton of their product we buy while that promotion is ongoing. During a one month special that could cost us two hundred dollars or more in contract payments. Accepting the loss of those dollars we decide to do it anyway, but that's not the end of the story. Let's say that Lorillard tobacco has a great deal on their Newport brand and we decide to take advantage of the special pricing. It's a good deal for our customers. When we put this special on the counter we must put an additional display from Phillip Morris on the same counter, displaying "Marlboros". That's in the contract. Our contract with RJ Reynolds requires us to put up a display of "Camel" cigarettes, so now we have three displays. But now we must give Phillip Morris a second display so they will retain their fifty percent of space. We are not done yet. The second display from Phillip Morris will be their price brand "Basic". This requires us to put a second display from RJ Reynolds featuring their price brand "Doral". Now we have to give one more to Phillip Morris so they can maintain their percentage. We now have six displays which will require at least six feet of counter space. We don't have six feet of space to give so we have to tell the Lorillard representative that we can't run the promotion. The contracts we have to sign restrict any chance of a rival tobacco company promoting their product and they know that. They have drafted these contracts with "unstated but designed consequences". The next time you're in a grocery store ask the manager if he is forced to display Coca-Cola when he promotes Pepsi or Tide detergent when he has Cheer detergent on sale. Tobacco companies should not be allowed to exert this much control over the market place.

The proposed legislation you have before you addresses two main points. It would prohibit a tobacco company from requiring a fixed percentage of category space for a retailer to contract. In our situation we would not be forced to give eighty-seven percent of our tobacco space to two companies. All stores could participate without regard to space and percentage considerations. A merchant could sell any or all of his space if he chooses to do so. A tobacco company could buy space or the best selling location if the merchant decides to sell, but could not tie that amount of purchased space to promotions or retailer incentives. The retailer would have the ability to make choices that will benefit his particular business.

The second point prohibits the contract from requiring a tie-in to any other promotion, such as the example I gave with the "Newport" display. Nothing in the legislation prohibits a merchant from having as many displays as he chooses. Nothing prevents him from accepting payments from the tobacco companies for these displays. He is not, however, forced to have six displays when he wants only one.

Without your help we have few choices. We can refuse to contract and try to compete with non-competitive prices. We know that is not an option. We can sit quietly, saying and doing nothing, and next year they will demand more as the competition grows weaker. You will hear someone tell you that we should take them to court if we believe they have engaged in unfair trade practice, antitrust or coercion. It took the states attorney generals years and millions of taxpayers' dollars to win the "Master Settlement Agreement". We don't have the money or the connections to pursue that option. We need your help.



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You will hear that this is a contract issue that does not need legislative interference. A contract is a "meeting of the minds", a give and take which should benefit both and be voluntarily entered into. They are so powerful, they do not negotiate. They sign you to a contract that makes it possible for you to continue in business.

They will say they are paying for shelf space. You can't sell them ten or twenty percent. Their contracts tell you the minimum they will accept. Someone may tell you that they are helping by showing us how to merchandise the tobacco category. How to help themselves at the expense of their competition is the result. The big get bigger and the small cease to exist.

A lobbyist for the "Retail Association of Nevada" will probably tell you that they disapprove of this legislation. We have been in business more than ten years and we had not heard of this association until we began working on this legislation. They obviously don't represent us. Perhaps they represent the large corporate offices that collect the contract dollars but never deal with the issues at a retail level. You will hear that the market place is full of contracts. That is true, but they are different. Contracts on candy, chips, soft drinks, and bread are common. Manufacturers buy the space they need to merchandise their product. The store can add footage to a category for other products if the need is there. We can add space likewise but the contracted companies take their percentage of that space also. Corporate retail executives fear that "paying for space" could be impaired if percentage contracts in tobacco were made illegal. Untold billions of dollars flow to corporate coffers as a result of slotting and merchandising payments. These dollars are not at risk with this bill. Tobacco companies will still pay these same dollars for premium placement, signage, and promotion.

You will probably hear from one lobbyist or another that their contracts do not limit competition in any way. I hope I have been able to persuade you that they do. The cumulative effect of even two contracts is devastating for competition.

The current situation is not good for the retailer, the consumer, or the long term health of the business climate. Left unchecked the giants of manufacturing may decide what consumers can buy and who they will buy it from. They may decide that one of your favorite products should be discontinued and replaced with one of theirs. Don't let this happen. True competition will give us the best products, the lowest prices, and a real choice in the market place.

Thank You,

David Jones

President,

PJ'S LIQUOR & WINE SHOP



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