
BAGGER V. DELISHCO

ARBITRATION

Fran Dalvera

**Purchasing Manager for
Delishco Beverage Products**

Witness Statement/Deposition Summary

You joined Delishco about 10 years ago after a stint in equipment and supply command and then purchasing for the Air Force. You report to Delishco's VP for Beverage Products. Pat Delahunt, whose mission it is to keep costs down and revenues up. Your job is to make sure that Delishco's suppliers are providing material and equipment that is high quality, serves the function well, and is delivered on time. While you negotiate the pricing and terms for smaller purchases, Pat Delahunt is often involved for larger dollar long term supply contracts with significant impact on the bottom line.

Of course, neither you nor Delahunt have complete autonomy within Delishco, a major international company with a myriad of product lines from food and snacks to personal care items. The company's CEO and senior management team direct overall business strategy, set growth and profit targets, and look for synergistic growth and profit opportunities between divisions.

Approximately two years ago, with Pat's approval, you sent out an RFP for a bag supply contract for your orange harvesting operations to a few large multinational bag manufacturing companies who supplied some of Delishco's other division.

Within a day or so after the RFP went out, Pat Delahunt came back from a Chamber of Commerce luncheon at which he happened to meet Sam Kremin of Bagger, Inc. He told you that he had offered Bagger the opportunity to bid on the RFP. Delahunt also commented that, according to Bagger's Sam Kremin, Delishco had been seriously over-paying for bags until that time. You were paying \$1.20 or \$1.30, but Kremin pegged the market price for any order larger than 100,000 bags at \$1.10 - \$1.15 per (depending on the size of the order), and he promised a significantly lower price on a much higher volume and an exclusive supply contract.

Delahunt told Kremin that even though Delishco hadn't favored "exclusives" in the past, they had tended to work with one supplier and that one has giving you lousy service and lousy bags. That's why the RFP was for an exclusive supply contract. Delahunt told you that Kremin pressed him for estimated volumes and at the time, he thought those ranged from 10 million to nearly 20 million per year. Based on those estimates, Kremin commented that you would reach 50 million bags in five years. For that, Bagger might go down as low as \$1.00 per bag.



A day or two later, Bagger submitted its formal bid proposal. In fact, even though one of the large multi-national suppliers cut its pricing to \$1.10 a bag for an exclusive contract, Bagger's bid price was the lowest at \$1.00 a bag. According to Delahunt, Sam Kremin seemed like a nice straight-up guy, and he said they would handle the volume. So, you emailed Sam that Bagger's proposal bid had been accepted, subject to negotiation of supply contract terms and conditions.

The negotiations were quite informal, taking place over a few phone conversations and emails [attached] with Sam Kremin. Early on, Sam requested, and you provided the schedule of Delishco's orange harvesting bag orders over the past five year. The bag order volume ranged from 7 million to 10 million per year, still high but not quite as high as Pat's off-the-cuff estimates.

You and Pat did negotiate once in person with Sam Kremin and his sales account manager, BJ Borman, about a week before the contract was written up and signed. The meeting took place when Kremin and Borman visited Delishco's orange harvesting facility. They had wanted to see how the oranges would be loaded, what stresses would be put on the bags, and to fine tune the sealing specifications.

After touring the harvesting facility, sandwiches were brought into the meeting. Pat had asked Delishco's general counsel's office to provide one of its inside lawyers for the meeting. As he explained, it made sense for the lawyer hear firsthand the business terms of the deal, since he would be writing up the contract. The lawyer who came seemed new and was pretty quiet throughout.

Until that meeting, most of the talk and emails had been about a five-year exclusive supply contract. However, at the meeting, Sam Kremin complained that, if the order history predicted the future, the low end of million bags a year, 5 years wouldn't add up to 50 million bags.

Ben Borman specifically stated: "Without a reasonable expectation of 50 million bag and exclusivity, Bagger can't stick to the \$1.00 per bag price. Sam stated that his dad - Bagger's owner "would never go for that. This discount is only on the table if we can get to 50 million bags. Even for large customer orders, but without exclusivity, our price would be at \$1.10."

You and Pat heard him loud and clear. To close the deal, Pat offered to take the exclusivity period out to 8 years, enabling them to reach their magic number of 50 million if the volume averaged 7 million bags a year.

At some point during the conversation, Sam had asked: "What if Delishco sells off its orange harvesting? Then what happens to the contract? Are there any plans for a sale?" Pat and the lawyer ACCURATELY stated that Delishco was not then planning



to sell its orange harvesting facility or operation. Pat also mentioned that Delishco was considering possible expansion to other fruits, which could mean more future business for Bagger.

Later, after the Bagger folks had left, Pat confided in you that, about 6 months earlier, he had attended an upper management meeting at which there was some discussion of at least half a dozen different strategic plans. One plan was labeled “Trimming the Vertical Chain” which talked about eliminating the lower end of vertical integration by spinning off operations that dealt with raw produce. Pat had heard nothing about it since then, and there was no mention of Vertical Chain in the Delishco President’s quarterly email report that came out a month or so later.

So, at the time of the meeting with Sam, Pat Delahunt didn’t think that spinning off the orange harvesting operation was still being considered. You saw no need mention it. It’s possible that the lawyer knew something about Delishco’s plans, but he didn’t tell you or Pat.

Pat explained that, if he had mentioned a spinoff as in the realm of possibility, Bagger would no doubt have insisted on a guarantee or pulled back on its price discount. If the corporate strategy types ever resurrected the spinoff idea, they would not be pleased by a guarantee tying Delishco’s hands for 8 years. Anything and everything can change in 8 years; Delishco has to be nimble.

About a week later, first thing in the morning, the lawyer sent Pat and you his draft of the Exclusive Supply Contract. Pat took a quick look and signed it on behalf of Delishco, and then sent it to Sam at Bagger, attached to an email that said: “here’s the formal contract, incorporating the terms we agreed upon in our meeting. As soon as you’ve signed it, we’ll send you our first order under the contract.”

Sam Kremin emailed it back, signed, almost immediately.

You do remember an email from BJ Borman a short while later. Borman’s email said: “Dear Fran, I am assuming you remember me from our meeting. I’m the Bagger representative working most directly on your account. I just want to make sure we’re on the same page because that young lawyer of yours left it murky in the contract. Before Bagger puts money into equipment, aren’t we agreed that Delishco plans to purchase a minimum of 50 million bags at this price, sometime in the next 8 years?”

You had a lot going on that day and were on your way out the door, but you read the email quickly and replied almost immediately: “On my way out, so short reply. I remember you. No worries - I think we’ll be at the 10 million level this year alone.”



The next time you spoke directly with anyone from Bagger was about six months after the contract was signed, Bagger Inc. hosted a celebration of its 75th year of business and invited many of its customers, friends, and current and past employees.

During the party, you briefly met Bagger's Terry Kremin, Bagger's CFO. He thanked you for Delishco's business, and said something like: "Well, we've now shipped the first 6 million or so bags and our machines just keep humming for Delishco." You remember saying something like: "I hope you keep it up, the quality of the bags and the efficiency of your service have been terrific." You remember Terry mentioning that his dad was excited about the magic number of 50 million bags. You remember saying: "at the rate we're going now, that should be possible."

About year into that contract, Pat was again pulled into strategic planning sessions at which the Vertical Chain Cutting idea was resurrected. The harvests of oranges and other citrus crops were considered to be unreliable due to changing weather conditions. A fruit harvesting company had approached Delishco with an offer for its harvesting operations, and Delishco decided to sell and let them deal with the raw food headaches.

They let you wait about six months longer until the end of the Florida growing season (and completion of the transaction) to inform Bagger. When the transaction was inked and the purchase complete, Pat told you to notify Bagger that Delishco would no longer require any bags as they no longer had any orange harvesting operations.

A few months later, you were not surprised to learn that Bagger had filed an arbitration claim.

It is true that over an 18-month period, Delishco purchased 15 million bags from Bagger, and everything worked well under the contract. Bagger's bags were of consistently high quality, delivered on time.