CPR INSTITUTE FOR DISPUTE RESOLUTION
ARBITRATION

In the Matter of

DAIRY QUEEN OPERATORS' ASSOCIATION and
DAIRY QUEEN OPERATORS' COOPERATIVE,

Claimants

vs.

INTERNATIONAL DAIRY QUEEN, INC., and
AMERICAN DAIRY QUEEN CORPORATION,

Respondents

AWARD and OPINION

Date of Award:
April 2, 2004

Before: Judith P. Meyer, Arbitrator

AWARD

The undersigned Arbitrator, having been designated in accordance with Section III.O.3 of the Class Settlement Agreement entered into by the parties on March 6, 2000, having been duly sworn, and having examined and considered the arguments, submissions, proofs and allegations of the parties, for the reasons set forth in the accompanying Opinion, finds, concludes and issues this Award as follows:

On the Requests for Relief by Claimants

1. **Respondents failed to provide specifications to Fabri-Kal in the form of the most detailed product specifications available, as required by the terms of the Class Settlement Agreement, §III.C.1.f.**

2. Respondents failed to apply reasonable product approval procedures in connection with the chocolate sandwich wafers supplied by Cookie Kingdom.

3. Respondents did not act unreasonably in providing a non-disclosure agreement to Lyons-Magnus. Claimants have the ability under the Class Settlement Agreement to secure a supply of non-disclosure agreements and control their dissemination to potential suppliers.

4. While having closer communications with its supplier, International Paper, than with Claimants' supplier, Maui Cup, Respondents did not unreasonably fail to advise Claimants in timely fashion regarding the Summer 2003 cup promotion. Maui Cup Company was in communication with Chromatic Technologies Ink as early as the week of January 26, 2003, within days after Respondents had determined the Summer 2003 promotion would utilize a U/V light reveal game element on the cup.

5. As to the claims that Respondents breached the Class Settlement Agreement by refusing to sell Claimants or DQOC-endorsed warehouses certain products:

a. As to Mr. Misty: Both Respondents and Claimants were unable to reproduce Mr. Misty flavors as supplied by Danisco, and there being therefore "no reasonable alternative", triggered the obligation of Respondents to sell Danisco flavors to DQOC-

endorsed warehouses at the same price and on the same terms that Respondents offer to their authorized warehouses.

b. As to <u>manufactured novelties</u>: Frostbite Brands is wholly owned by Dean Foods and Dean Foods sells to Respondents within the meaning of §III.E.3 (1). Should there be no other "reasonable alternative" to the supply of manufactured novelties other than Frostbite Brands, Respondents will sell to DQOC-endorsed warehouses at the same price and on the same terms that Respondents sell to IDQ-authorized warehouses.

c. With respect to the <u>Ultimate Box</u>, the matter is mooted by Claimants continued search for an alternative supplier and Respondents subsequent elimination of the product. The matter was ripe for arbitration in November 2001 and is no longer.

d. With respect to the <u>Keebler® Fudge Stripe Cookie</u> Blizzard® flavor, the evidence does not support a finding that Keebler Fudge Stripe Cookies were unavailable, since had Tarrier placed its order in December 2002 or January 2003 the product might have been delivered in time for the promotion. Claimants requested specs for only *non-branded* products in December 2002 and did not ask for Keebler® specs until January 21, 2003.

6. As to the specifications for new products, the Arbitrator finds that Respondents sent the specifications for certain products more than 5 business

days after finalization: Respondent sent the specs for Bubble Gum Popping Candy 14 calendar days after finalization; the specs for Caesar Salad dressing 47 calendar days after finalization; and the specs for Green Apple Topping 8 calendar days after finalization.

<u>With respect to the Request for Relief by Respondents</u>

To the extent that Respondents requests have not been dealt with by the findings above, the Arbitrator finds:

1. **The Agreement does not address and therefore does not preclude IDQ from requiring its warehouses carry whatever supply of IDQ product it negotiates with that warehouse, and, to the extent any such requirement might violate other terms of the Agreement in future specific circumstances is not decided here.**

2. **Claimants did not present sufficient probative evidence relating to delay caused by changes in the graphics of cone jackets, and the evidence presented supports the finding that changes in cone jacket graphics were less problematic than start-up problems with cone manufacturing machinery whose operation Claimants struggled to perfect in Elizabethtown, Kentucky.**

3. **The evidence presented on whether the majority of LTOs covered by §III.E are branded products, while statistically probative, does not answer the question of whether Claimants may seek alternative processors for branded**

products when incorporated in Dairy Queen® products in an altered state. A trademark or brand is a distinctive name identifying a product or a manufacturer that in the mind of the consuming public equates to a certain quality and style. The mark or brand connotes a measure of uniformity in the public mind which attaches to the usual form in which the product is sold to the consumer. If the product is included in an LTO in a form in which the public does not primarily associate it, such as a grind, Claimants may seek an alternative processor to prepare the final-use state of the branded product.

The Arbitrator apportions the fees of the Arbitrator equally between the parties. Each party shall bear its own costs and attorneys' fees.

OPINION ON AWARD

I. Introduction and Procedural Statement

The parties entered into a Class Settlement Agreement (the "Agreement") on March 6, 2000. Section III.O of the Agreement establishes a dispute resolution procedure providing for arbitration of disputes arising under the Agreement. Pursuant to §III.O.3, the parties appointed a Standing Arbitrator in August 2000. On June 9, 2003 Claimants filed a Demand for Arbitration requesting an arbitral declaration that *inter alia*:

1. Respondents breached the Agreement "by failing to fairly and evenly administer the product approval process and by failing to 'help facilitate increased competition and product cost control for products used in Dairy Queen stores'" under §II of the Agreement;
2. That Claimants have demonstrated that there is "no reasonable alternative manufacturer" under §III.E of the Agreement for certain items used in Dairy Queen products;
3. A determination of the meaning of "branded" products as used in §III.E.3 of the Agreement;
4. A determination that with respect to certain products, Respondents are required to sell these products to Claimants or their suppliers or endorsed warehouses at the same price and terms as Respondents' suppliers sell to Respondents;
5. A determination that Respondents have breached obligations set forth in the Agreement and have failed to "exercise good faith and act reasonably in applying the product approval procedures" under §III.C.1.a and have failed to respect and to cooperate in good faith with Claimants in the advancement and improvement of the Dairy Queen system.

Respondents filed a Response and Counter-Demand on September 24, 2003.

For their part, Respondents requested the Arbitrator find *inter alia* that:

1. Respondents have not breached the Agreement; and that
2. Claimants failed to honor the spirit and goals of the Agreement; failed to demonstrate respect for Respondents; and failed to comply with the product approval procedures of the Agreement.

The parties appeared in arbitration in Minneapolis, Minnesota on December 6 to 10, 2003 and on January 26 and 27, 2004.[1] At the conclusion of the testimony, each side stating that it had no further evidence to offer, the matter was argued by counsel and, after post-arbitration briefing, was submitted for decision on March 15, 2004. In their Post Arbitration Memoranda and Replies, based on their respective beliefs of what the evidence showed, the Parties refined their requests for relief. Claimants now seek an Order declaring Respondents breached the Agreement in the following particulars:

[1] Pursuant to §III.O.2 the Parties chose arbitration under the authority of the Federal Arbitration Act 9USC§1*et seq*.

By failing to act in good faith and reasonably applying product approval procedures in connection with Fabri-Kal's manufacture of plastic dishes and in connection with chocolate sandwich wafers manufactured by Cookie Kingdom; in requiring Lyons Magnus to sign a separate new non-disclosure agreement; by failing to advise Claimants in timely fashion regarding new product developments, particularly with respect to the Summer 2003 cup promotion; by refusing to sell Claimants or DQOC-endorsed warehouses Mr. Misty flavors, Manufactured Novelties, the Ultimate Box, and Keebler Fudge Strip Cookie Blizzard® flavor at the same price and on the same terms that Respondents offer to IDQ-authorized warehouses; failing to provide timely specifications for new products with respect to Bubble Gum Popping Candy, Caesar Salad Dressing and Green Apple Topping. Claimants ask the Arbitrator to enter an Order requiring Respondents to sell the DQOC-endorsed warehouses Mr. Misty flavors, Manufactured Novelties and LTO products, which DQOC-endorsed manufacturers are unable to produce in time to participate in an LTO, at the same price and the same terms as IDQ-authorized warehouses.

On their side, Respondents ask the Arbitrator to find that:

Section III.E of the Agreement does not apply to the majority of LTO's which are third-party branded products; that III.F of the Agreement applies to all LTO's but that Claimants did not exercise due diligence in securing their own independent manufacturer of LTO's other than the Keebler Fudge striped cookie product and in that circumstance were dilatory in asking their existing Blizzard® ingredients grinder, Tarrier, to order product; that nothing in the Agreement precludes IDQ from requiring its warehouses carry an adequate supply of IDQ product to meet demands of franchisees; that there existed "reasonable alternatives for the Ultimate Box, manufactured novelties and hamburger patties and that any Mr. Misty product claim has been mooted by Respondents securing Beck flavorings for Kosto; that the discrepancy in plastics drawings provided Fabri-Kal was not due to Respondents' misconduct and had, in any event, no adverse impact on Claimants' ability to get the product to market; that Respondents had good reason to change the graphics for the cone jackets and that graphics changes were timely transmitted; that Respondents did not breach the Agreement in its dealing with Maui in the 2003 summer cup promotion; and that the Claimants have admitted that they failed to show respect for Respondents. Affirmatively, Respondents ask the Arbitrator to order the Claimants to demonstrate respect in the future.

The Arbitrator first commends Counsel for both parties for the extraordinarily capable and ardent advocacy demonstrated on behalf of their respective clients and the laudable professionalism with which they conducted themselves during the arbitration.

II. Background

International Dairy Queen ("IDQ") is a wholly owned subsidiary of Berkshire Hathaway, Inc. American Dairy Queen Corporation ("ADQ") is a subsidiary of IDQ. [2] An American success story, IDQ began with a single product in a single Midwestern store before World War II. Now one of the largest fast food systems globally, more than 5900 stores operate nationally, in Canada, and internationally under the Dairy Queen® name. IDQ franchises the Dairy Queen system and sells food products and supplies to franchisees. Dairy Queen Operators' Association ("DQOA") is a voluntary membership association of dues-paying Diary Queen and Dairy Queen/Brazier[3] franchisees. Dairy Queen franchisees created the Dairy Queen Operators' Cooperative ("DQOC"). The DQOC negotiates directly with independent manufacturers for Dairy Queen-approved product at prices lower than those charged by IDQ to its franchisees.[4]

As the franchise system matured, the relationship of IDQ and the DQOA grew rocky and conflictual. In 1994, five Georgia franchisees sued IDQ for federal anti-trust violations, alleging that IDQ's approved supplier program and procedures constituted a prohibited

[2] The Arbitrator will refer to International Dairy Queen, Inc. and American Dairy Queen Corporation collectively as IDQ or Respondents, except as otherwise indicated.
[3] IDQ introduced the Dairy Queen/Brazier product line nationally in 1968. The Brazier product line features hamburgers, hot dogs, chicken strips and chicken barbeque, French fries and onion rings.
[4] The Arbitrator will refer to the DQOA/DQOC collectively as the DQOA or Claimants, except as otherwise indicated.

tying arrangement, a breach of contract and a breach of the implied covenant of good faith and fair dealing between the parties. Failure to act in good faith is behavior both parties now claim against each other. The current charge is seeded in the mistrust that engendered the *Collins* litigation, festered during its pendency, briefly abated with its settlement, and then rekindled as the parties ventured to work cooperatively.[5]

The parties in their Agreement "recognize that they will benefit if they work together, whenever reasonably possible, for the good of the Franchisees and the franchisor in the Dairy Queen system." The franchisees entered into the Agreement "in an effort to establish procedures that will help facilitate increased competition and product cost control for products used in Dairy Queen stores." Importantly, IDQ recognizes that "IDQ's franchisees operate in a highly competitive market place. If their products cannot be priced competitively, franchisees are out of business. If franchisees are out of business, IDQ is out of business."[6] Nor do Claimants disagree. "The franchisees have significant personal and financial investments in their Dairy Queen businesses, and a strong Dairy Queen franchise system benefits the franchisees…"[7]

Six years after *Collins* began, the parties resolved their differences. In their Agreement, the parties

> "recognize that they will benefit if they work together, whenever reasonably possible, for the good of the Franchisees and the franchisor in the 'Dairy Queen'

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[5] *Collins* was not the first skirmish between the parties. Friction between IDQ and its franchisees erupted decades earlier, in another class action entitled, *Charles Poole v. American Dairy Queen Corporation* which settled in 1974. The terms of the *Poole* Class Settlement Agreement were specifically superceded by the Agreement *Collins* generated.
[6] IDQ Post Hearing Memorandum, p. 57.
[7] Claimants' Response to IDQ/ADQ Post Hearing Memorandum, fn.2.

> system. The Named Plaintiffs (individually and as representatives of all class members) enter into this Settlement Agreement in an effort to establish procedures that will help facilitate increased competition and product cost control for products used in 'Dairy Queen' stores. The Named Plaintiffs believe that, at this time, the best solution to help ensure increased competition and product cost controls is through a viable DQOA/DQOC-endorsed and DQOC-affiliated manufacturers and suppliers and IDQ-authorized or affiliated manufacturers and suppliers."[8]

The franchisees' belief that IDQ does not share the concept of increased competition as a "best solution" is the friction generating this arbitration. As noted, *Collins* was not the first skirmish between the parties.

In an effort not to repeat the past and to put in place a new protocol governing the product approval process, the parties established what they hoped were bullet-proof procedures that would allow DQOA, in the words of the Agreement, to "develop, administer and provide a distribution system for the purchase, sale and distribution of products to Dairy Queen store operators [and] warehouses" and the "right to participate in the distribution of products by…buying products and reselling [them] at a profit to Dairy Queen store operators [and] warehouses…or endorsing manufacturers and processors of products…"[9] Affirming its long-held position, at the same time IDQ asserted it had no "obligation to develop, administer, or provide a system for the distribution of products to store operators in the Dairy Queen system…" and that it "do[es] have the right…to develop, administer, and provide a distribution system for the purchase, sale, and distribution of products to 'Dairy Queen' store, operators, warehouses…" and "the right to…[buy] and [resell] those products at a profit to 'Dairy Queen' store operators, warehouses and others."[10] To yoke

[8] Agreement, §II.
[9] Agreement, §III.B.
[10] Agreement, §III.B.

the perceived tension between the dynamic “right” of the DQOA and the feared passive-aggressive resistance of IDQ, the parties set forth a Product Approval Process with a mix of commanding timelines, attitudinal requirements and dispute resolution procedures. The pertinent language of the Product Approval Process is set forth below:

III.C. Product Approval Process

1. ADQ has established certain procedures and policies for the approval of food products, ingredients sold to store operators for use in their preparation of food products and consumer packaging for food and drink products sold or used in the “Dairy Queen” system…

   a. IDQ/ADQ will exercise good faith and act reasonably in applying the product approval procedures, including its determination concerning the conformance of Products with its specifications and/or standards…

   d. IDQ/ADQ will, within ten (10) business days after its receipt of a written request from a Franchisee or its designated agent, provide the summary specification for a particular Product…

   e. IDQ/ADQ will, within seven (7) business days after its receipt of a written request from a Franchisee or its designated agent, send a proposed manufacturer or processor a non-disclosure agreement…

   f. IDQ/ADQ will send product specifications and, when appropriate, a sample control Product to a manufacturer or processor…within seven (7) business days after IDQ/ADQ’s receipt of a completed non-disclosure agreement…

   j. If a Product sample that is submitted by a proposed alternative manufacturer or processor and evaluated by IDQ/ADQ deviates only minimally from IDQ/ADQ’s product specifications and poses no health or safety issues to consumers or others IDQ/ADQ will not unreasonably withhold their consent to allow the proposed manufacturer or processor to distribute the Products from the production run from which the test sample was taken, to the Dairy Queen system…

E. Certain Product Specifications

1. In the event that DQOA/DQOC request approval for a manufacturer or processor of a Product that is a menu item or an ingredient or consumer packaging for a menu item that is approved for use in the Diary Queen system, and DQOA/DQOC certify that the Product is covered by the Section III.E and that there is not a ‘reasonable alternative manufacturer or processor’ other than the manufacturer or processor who sells the Product to IDQ/ADQ, IDQ/ADQ shall, after determining that the Product is covered by

> this Section III.E and that there is not a ‘reasonable alternative manufacturer or processor’ for the Product, elect either to:
>
> a. Approve an additional manufacturer or processor that does not sell Products to IDQ/ADQ and offers a functionally equivalent Product, which may not meet IDQ/ADQ’s specifications; or
> b. Sell the IDQ/ADQ Product directly to DQOC-endorsed warehouses or manufacturers/processors at the same price and on the same terms that the Product is sold to IDQ/ADQ-authorized warehouses…until such time as there is an available ‘reasonable alternative manufacturer or processor’ or IDQ/ADQ approves a functionally equivalent Product…
>
> 2. The term ‘reasonable alternative manufacturer or processor’ shall be defined as a manufacturer or processor of a Product…other than a third party’s branded Product, that: (1) does not sell Products to IDQ/ADQ; and (2) does not need to invest in major equipment in order to be capable of manufacturing or producing the Product to IDQ/ADQ’s specification.

At the time of the *Collins* settlement, both parties, exhausted from years of fighting, sought to make acrimony a thing of the past. To that end, the parties expressed mutual hope for a better relationship.

> **III.M** **<u>Mutual Respect and Cooperation.</u>**
>
> …A significant portion of the consideration for the Settlement Agreement is to eliminate the disruptions and impairments that the Lawsuit and the disputes between the Parties have imposed on their activities and the ‘Dairy Queen’ system generally…IDQ/ADQ and the DQOA/DQOC agree to demonstrate mutual respect for one another and to cooperate in good faith with one another for the advancement and improvement of the ‘Dairy Queen’ system…

III. THE PRESENT DISPUTES

The parties executed the *Collins* Agreement on March 6, 2000. Within the year, events began to occur which, when viewed through the IDQ prism, were capable of innocent

explanation. These same events, viewed through the DQOA prism, evidenced IDQ's intent to frustrate the Agreement. And not only to frustrate the Agreement but to return to actualizing what DQOA has always believed to be IDQ's motiviating desire: to monopolize the sale of Dairy Queen approved products to Dairy Queen franchisees. Because the DQOA provides IDQ's sole source of competition, and resultant reduction in franchisor profits, and because of the history the parties share, DQOA experiences frustrations under the Agreement as not only intentional but the result of broad corporate mandate. Here, although principal marketplace competitors, the parties form a symbiotic relationship. Neither can survive without the other. Like a marriage where divorce is impossible and communication is poor, words and actions are felt as hurtful and therefore believed to be so intended. Joined at the hip, the franchisor definitionally requires the existence of its franchisees and depends on them for its profit; the franchisees exist solely because of the franchisor and profit by the goodwill of its name and the popularity of its menu. And yet, within the closed system of Dairy Queen, the franchisor and franchisees compete aggressively for the same products.

The parties often agree on the same set of facts that, when nuanced and interpreted through the lens of mutual distrust, give rise to differing interpretations: on IDQ's side, one of unusual circumstances colliding; for DQOA a story of subterfuge and bad faith. That said, the parties do agree on one breach of the Agreement: IDQ sent specifications for new products that were part of LTO promotions more than 5 business days after IDQ finalized the specifications.[11] To wit, IDQ sent the specifications for Bubble Gum

[11] Section F.2 of the Agreement requires ADQ to provide specs for new products "within 5 business days after ADQ finalizes the specifications."

Popping Candy 14 days after finalization; IDQ sent the specs for Caesar Salad dressing – finalized on December 13, 2002 and forwarded on January 30, 2003 -- 47 days after finalization of specifications [Claimants' Ex. 84, 85]; and IDQ sent Green Apple Topping specs 8 days after finalization (finalized on 2/11/03 and sent on 2/19/03) [Claimants' Ex. 85].

A. Product Approvals: Fabri-Kal and Cookie Kingdom

1. Fabri-Kal

One set of events on which the parties heartily disagree surround Fabri-Kal's efforts to manufacture sundae cups for the DQ system. First approached by DQOC's director of purchasing and distribution, Josh Schmieg, in late June 2000, Fabri-Kal expressed interest in manufacturing for the DQOA. On October 4, 2000 Harris Cooper notified Glenn Lindsey that DQOA had selected Fabri-Kal as its supplier of thermoform and injection molded plastic products. [Claimants' Ex. 8] On October 26, Cooper requested IDQ "to move to the second stage and continue with the product approval process with Fabri-Kal." [Respondents' Ex. 175] On October 30, IDQ quality assurance manager, Jennifer Fredenburg, sent control samples to Fabri-Kal's David Asarnow, noting "these control samples has [sic] not been tested by our Quality Assurance department. If the control sample deviates from the specification, the product specification takes precedence over the control sample." [Claimants' Ex. 10; Respondents' Ex. 176]

Fabri-Kal began duplicating the engineering drawings received from IDQ, but in reviewing their output at a management meeting at their Kalamazoo plant on December

3, 2000 became concerned that the IDQ drawings did not match the WNA Comet samples provided. [Testimony David Asarnow] On January 23, 2001 Fabri-Kal's engineer and project manager, Rod Henderson, called IDQ senior food technologist, Nicole Matzke and told her the IDQ drawings did not match the IDQ samples. On January 25, 2001 David Asarnow and Rod Henderson met with IDQ vice-president of research and development, Glenn Lindsey, and Nicole Matzke in Minneapolis. Henderson brought with him revised drawings (based on the WNA Comet samples).

At the meeting, IDQ acknowledged that the drawings, originated by IDQ's supplier WNA Comet, were inaccurate, although until Fabri-Kal brought it to IDQ's attention in the phone call of January 23, Glenn Lindsey did not know that the drawings sent were not the most recent. IDQ promised revised production drawings from WNA Comet and meanwhile suggested that Fabri-Kal build a container based on the WNA Comet sample.

Was IDQ's failure to provide accurate specs intentional, in bad faith and part of an effort to frustrate DQOA's ability to acquire Fabri-Kal as a supplier? The Arbitrator need not make so broad a determination and the evidence on the subject is equivocal. It is sufficient to point out that Section III.C.1.f of the Agreement requires specs to be in the form of the most detailed product specs available to Respondents. The contractual conundrum becomes: were the WNA Comet specs "available" to IDQ? Which generates the next question: what is the duty, if any, of IDQ to assure itself that specs it provides "are in the form of the most detailed product specifications available?" Presumably WNA Comet's revised product specs were "available" had IDQ asked, and, indeed, when

IDQ did ask, WNA Comet made its revised specs quickly available. Without express direction, Fabri-Kal took a risk in building a container based on the WNA Comet sample provided, as Glenn Lindsey would not assure that samples sent Fabri-Kal were accurate prototypes.

Although IDQ directed Fabri-Kal that product specifications took precedence over control samples, Glenn Lindsey was unaware that WNA Comet had changed its specs and not submitted its changed specs to IDQ for necessary approval. Once advised, Glenn Lindsey called WNA Comet; they apologized for not clearing their changed specs with IDQ explaining that while they had changed the stacking lugs on the containers, they did not know that IDQ would be sending out their product to anyone else. At the January 25, 2001 Minneapolis meeting Glenn Lindsey promised to get revised production specifications from WNA Comet to Fabri-Kal. At that same meeting, Fabri-Kal expressed concern that it would be held to a higher standard than WNA Comet. Glenn Lindsey assured Fabri-Kal that IDQ would not favor its own supplier. By letter of January 30, 2001, Glenn Lindsey both approved the revised drawings that Fabri-Kal brought to the January 25 meeting and sent out revised control drawings and control product specs of the small, medium and large sundae cups and parfait glasses along with a revised product spec for the banana split dish. IDQ also approved Farbi-Kal's use of a different resin with the exception of the ingredient XK40. [Claimants' Ex. 13] Fabri-Kal ended up scrapping $13,000 of corrugated material because it wanted to duplicate WNA Comet's horizontal packing of the parfait cups[12] and spent an additional $20,000 to

[12] David Asarnow felt that IDQ was showing favoritism when Fabri-Kal learned that WNA Comet packed the small sundae cup horizontally rather than vertically, although Nicole Matzke allowed that Fabri-Kal

remove the "patent pending" disclaimer on the bottoms of product when, in April 2001, IDQ ended its pursuit of a patent.[13]

IDQ expressed surprise and dismay upon learning that WNA Comet had changed its specs without consultation with or approval by IDQ. Nothing in the testimony leads the Arbitrator to conclude that IDQ intentionally misled DQOA or intentionally delayed the approval process by sending out superceded specifications for a product. However, IDQ did contravene the Agreement. Section III.C.1.f requires IDQ to provide specs "in the form of the most detailed product specifications available to IDQ/ADQ." While IDQ did not possess the most detailed product specs in December 2000, no one argues these specs were unavailable. Indeed, when IDQ asked for these specs, it got them. Prudence, and compliance with the Agreement, might suggest that IDQ verify it possessed the most detailed specs (which the Arbitrator also reads as "current") before transmittal to a supplier who expects to rely on them.[14] That Fabri-Kal is a sophisticated manufacturer who discovered the discrepancy quickly is all to the good. It does not excuse IDQ from compliance with the duty of the Agreement in the first instance.

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could use its already purchased boxes and pack 936 cups rather than 1000 per box. IDQ sent Fabri-Kal case dimensions used by WNA Comet on January 30, 2001 [Respondents' Ex. 183] for information purposes; the dimensions used by Comet were not required. The packing specs themselves, while indicating a case pack of 1000 count, do not dictate vertical or horizontal packing.

[13] Claimants make no monetary damage claims in this arbitration. The testimony suggests that DQOA suppliers did not, at least directly, pass on such costs to Claimants.

[14] WNA Comet's alleged "defense" that it did not provide the revised specs to IDQ because it did not know that a third-party might rely on them misses the mark. First of all, an IDQ supplier's assumptions are irrelevant to the instant dispute and do not supply an affirmative defense. Secondly, it is IDQ policy that it must approve any and all changes to IDQ specs and a supplier should be well aware of that requirement.

3. **Cookie Kingdom**

Josh Schmieg, director of purchasing and distribution at DQOC, was looking for a chocolate wafer sandwich cookie that it could offer storeowners as an alternative to the IDQ-supplied wafer used in the DQ® Sandwich. Cookie Kingdom contacted Schmieg, and DQOA initiated the approval process with IDQ sending Cookie Kingdom a non-disclosure agreement. On June 18, 2001 Harris Cooper asked IDQ to sent specs to Doug Willis at Cookie Kingdom. [Claimants' Ex. 60] After return of the non-disclosure agreement, on June 20, 2003, IDQ sent product specs to Doug Willis. [Respondents' Ex. 150] On July 21, 2001 IDQ sent a control sample not tested by Quality Assurance. [Claimants' Ex. 61] On July 30, 2001, Cookie Kingdom sent IDQ a sample of its current scalloped three-inch chocolate wafer, indicating it would purchase a die roller to match the IDQ logo if approved. Noting that the ingredients declaration on Cookie Kingdom's product did not match IDQ's label, IDQ declined review of the submitted sample.

IDQ's product specifications, per its product specification sent on June 20 with an effective date of 6/19/03, dictated a label declaration of: "bleached wheat flour, sugar, vegetable shortening (partially hydrogenated oils: soybean, cottonseed), high fructose corn syrup, caramel color, baking soda, cocoa, soy flour, salt, soy lechtin (emulsifier), artificial flavor. The IDQ product spec formulation by weight was: "bleached flour, sugar, vegetable shortening, high fructose corn syrup, water, caramel color, and less than 1% of leavening (sodium bicarbonate), cocoa, soy flour, salt, soy lechtin and artificial flavor. The declaration on an IDQ box from 03/99 [Claimants' Ex. 64] lists "enriched

wheat flour"; the same box from an 09/03 production run, containing 6 individually wrapped DQ® Sandwiches, lists "bleached wheat flour"[Respondents' Ex. 156A].

According to Glenn Lindsey, IDQ changed the DQ® Sandwich ingredient from "enriched wheat flour" to "bleached flour" sometime between 1999 and 2003. Boxes with the old product description remained in circulation until supply was depleted. The box with the new ingredient listings came out, according to Lindsey, in July 2003. The Cookie Kingdom product includes "enriched wheat flour" which matches the IDQ product description in circulation until June 2003 and includes vanilla (presumably less than 1%) which the IDQ formulation lists only as "artificial flavor", but does not identify as vanilla. The ingredient declarations of the two products are listed in slightly different order. IDQ lists vegetable shortening before high fructose corn syrup and Cookie Kingdom lists shortening afterwards. IDQ describes vegetable shortening as partially hydrogenated soybean and/or cottonseed oil and CK lists only soybean oil.

Other than the varying description of "wheat flour" (CK) [Respondents' 155, 155B] vs. "bleached wheat flour" (IDQ), the order of ingredients and the choice of wording, it is not clear that the Cookie Kingdom product is, in fact, different from the IDQ product formulation either prior to or after June 2003. The Arbitrator, without expert opinion, cannot opine whether "bleached wheat flour" and "wheat flour" (or "enriched wheat flour" for that matter) are materially different ingredients or whether more or less vegetable shortening or corn syrup make one product not the functional equivalent of the other. Glenn Lindsey, however, wrote Cooper on August 25, 2003: "If we were to

approve a wafer with a different ingredient declaration, this would create inconsistent quality and we would have to provide two DQ sandwich bags to our stores." [Claimants' Ex. 66] At the time IDQ was supplying stores with boxes bearing ingredient listings different from the listings on the bags enwrapping the product, but phasing out the boxes bearing the superceded description. The bag listed ingredients accurately as of July 2003, but because of the difference between IDQ specs and Cookie Kingdom's, IDQ did not test the Cookie Kingdom cookie for its organoleptic characteristics.

Although IDQ asserts that it could not "by federal law, approve a new sandwich wafer that did not have the same basic ingredients as the existing wafer",[15] that statement begs the question. Agreement §III.C.1.j requires that "[i]f a Product sample that is submitted by a proposed alternative manufacturer or processor and evaluated by IDQ/ADQ deviates only minimally from IDQ/ADQ's product specifications and poses no health or safety issues to consumers…IDQ/ADQ will not unreasonably withhold their consent…" IDQ did not carry its burden of proof to demonstrate that, in fact, bleached wheat flour differs materially from wheat flour and/or that the one-place difference in the listing of shortening is a difference posing a consumer health or safety issue or a difference disallowed by law.

B. <u>New Product Development</u>

Section III.F.2 addresses new products. IDQ, "as the franchisor in the 'Dairy Queen' system, has the right to continue to develop new Products… ADQ will provide

[15] IDQ/ADQ Reply Memorandum, p. 23.

notice…within seven (7) business days after the date of the advisory council meeting at which the [new product] recommendation was made…If the DQOA/DQOC have an interest in submitting an alternative manufacturer or processor for the new Product, they may submit the name and address of the proposed manufacturer or processor, and the name of the contact person, to ADQ in writing, together with the non-disclosure agreement…ADQ will provide monthly progress reports to the proposed manufacturer or processor and the Executive Director of the DQOA concerning the development and possible introduction of the proposed Product. ADQ will provide Product specifications for new Products…within five (5) business days after ADQ finalizes the specifications." Section 4 allows, if the proposed manufacturer has proceeded with due diligence in the new product development process but cannot finalize the new product on its introduction date, that IDQ will then sell the new product to DQOA endorsed warehouses for the shorter of 60 business days after the introduction date or 20 business days after the DQOA-endorsed manufacturer's product is approved.

1. The 2003 Summer Cup Promotion

On January 8, 2003 Patty Halvorson, Director of National/Local Promotions, wrote Harris Cooper about the "Turn America Upside Down Promotion – Instant Win Cup" to run in July and August 2003 featuring a 16-ounce cold reveal cup or, possibly, a U/V light reveal or peel-and-win. The cup required special ink to be developed by Chromatic Technologies Ink ("CTI"). Halvorson identified contact person, Glenn Small, at CTI. Her letter included a preliminary cup mock-up, prepared by International Paper, which included a blank oval for the cold reveal. Halvorson copied the letter and the layout to

David Ward, Maui Cup's Midwest Regional Food Service Business Manager, and David Bradwell, Ward's boss, at Maui Cup Company, DQOA's cup supplier. [Claimants' Ex. 18; Respondents' Ex. 190] The Ryan Partnership, a promotional idea company consulting to IDQ, knew that CTI had ink reactive to cold. Halvorson herself had some initial conversations with CTI in October 2002. Halvorson also talked to International Paper, IDQ's cup supplier, in October 2002 because IP had never done a cold reveal before. It was also IDQ's practice to pull IP into discussions when technical questions were raised. Between the November FAC meeting and a January 22 FAC conference call, CTI came up with the idea of a light reveal. CTI told Halvorson that any cup manufacturer could do these cups so long as it purchased a special Flexo ink. Halvorson testified that she told Dave Randall at CTI about Maui in October 2002. In contradiction, Maui's David Ward testified that CTI only learned in February that Maui was an additional cup supplier. The evidence shows that Dave Randall of CTI contacted Dave Ward at Maui during the week of January 26, 2003 and that there were "numerous conversations between Maui Cup and CTI" after that time. [Respondents Ex. 211, 212] IP prepared mock-ups of the coatings on the cups and the ink for show at the FAC meeting in February 2003.

On January 17 Harris Cooper wrote Mike Rinke announcing DQOC's participation in the Instant Win Cup promotion and asking Rinke to "provide the necessary materials to David Ward, Maui Cup Company in order to initiate this process." [Claimants' Ex. 19; Respondents' Ex. 191] On Friday, January 24 Rinke wrote Cooper that after a telephone conference call on Wednesday, January 22 with FAC, "[w]e've decided to move forward

with a U/V light reveal game element on the cup." Rinke confirmed that IDQ would continue working with Maui on the details and that Maui would print 9 million of the special 16-ounce cups.

On February 14, 2003 Halvorson e-mailed David Ward at Maui Cup with contact names for the cup graphics pointing him to Dave Randall at CTI for questions on the special ink required for the cups. [Respondents' Ex. 199] On Wednesday, February 19 Ward e-mailed back that everything was moving on his end and he would provide Halvorson with a timeline on Friday. [Respondents' Ex. 201] But on February 24, Ward discovered that Maui would require water-based Flexo ink for the cups. Maui was set up to use only oil-based offset ink and Flexo ink required different printers. International Paper can print an 8-color Flexo, and while Maui had a 4-color Flexo printer, it could not print the 2003 promotional Blizzard cup. Ward called Halvorson three or four times during the week of February 24 and on March 3 with no response. On March 4 Ward e-mailed Josh Schmieg that UV Reveal ink for offset printing would be available but that it might not have enough pigment to be usable and that CTI was just informed "a couple of weeks ago" that Maui was the second cup supplier in the DQ system. Halvorson returned Ward's calls after 5 p.m. on March 5 at which time Ward told Halvorson that Maui used a different ink but was looking at other ways of getting the promotion done. On Thursday, March 13 Ward e-mailed Halvorson confirming Maui's participation and informing her "[o]ur graphics manager Gary Jagod will continue to communicate with Dave Randall at CTI to make the necessary arrangements for the shipment of the special ink." [Respondents' Ex. 213]

On March 7, Mike Rinke wrote Harris Cooper, reminding him that on January 23 Maui had committed to 9 million cups, had confirmed this number on January 24, and that "[i]f we incur any problems because of Maui's failure to participate in the promotion, we will look to Maui and the DQOC to reimburse any losses." [Claimants' Ex.30; Respondents' Ex. 210] On March 20, David Bradwell, Director of Maui Sales, wrote Josh Schmieg that Maui would outsource its 9 million cups [Claimants' Ex. 30] and on March 26 e-mailed Ryan Partnership that Halvorson would have proofs to approve the following week. [Claimants' Ex. 35]

Respondents contend that Maui was not diligent in discovering its needs from CTI or in ordering the necessary curing equipment needed to produce either the cold reveal or the U/V light reveal cup. Claimants contend that CTI had worked with IDQ and International Paper for months before bringing Maui into the loop and that Maui only became aware of its needs on February 24. The evidence, however, shows that CTI contacted Maui on January 26. On January 22, after a FAC conference call, IDQ committed to the U/V light reveal and wrote DQOA its decision on January 24. While there were discussions between IDQ and International Paper in October 2002, nothing in the evidence suggests that IDQ committed to the U/V light reveal before January 22, 2003. If this is the case and if CTI called Maui on January 26, it appears that Maui may have dropped the ball by failing to ask the right questions of CTI or CTI may have dropped the ball by making assumptions regarding the capabilities of Maui. The evidence suggests rampant miscommunication, but not nefarious dealings.

C. No Reasonable Alternative Manufacturer

Under the Agreement, §II.E.3 a “reasonable alternative manufacturer or processor” is one that “does not sell Products” to IDQ and “does not need to invest in major equipment” in order to manufacture the product to IDQ specifications. And if there simply is no “reasonable alternative manufacturer”, then under §III.E.1 IDQ must either approve an additional manufacturer that does not sell to IDQ and offers a “functionally equivalent Product” or “[s]ell the Product directly to DQOC-endorsed warehouses or manufacturers/processors at the same price and on the same terms that” IDQ sells to IDQ authorized warehouses…” Before this is done, DQOA “shall designate, in writing, the steps…that [it has] taken to locate a ‘reasonable alternative manufacturer or processor’”. IDQ may then within 20 business days submit its position on the product in issue and the names and addresses of potential manufacturers or processors of the product. [Agreement §III.E.5a,b]. At that point, if the DQOA still disputes that a reasonable alternative manufacturer exists, the DQOA may submit the dispute to arbitration. Section III.E.3 excludes third party branded products from the products that can have functional equivalents through production by a reasonable alternative manufacturer or processor.[16]

1. Mr. Misty Flavors

Danisco produces proprietary flavors for IDQ. It keeps these formulae in escrow for IDQ. IDQ itself has tried to match Danisco’s flavors with no success and has turned to

[16] Section III.E.3: “The term ‘reasonable alternative manufacturer or processor’ shall be defined as a manufacturer or processor of a Product that is a menu item or an ingredient or consumer packaging for a menu item that is approved for use in ‘Dairy Queen’ stores, other than a third party’s branded Product…”

CocaCola to reproduce Danisco's product. Coke came up with a blue raspberry flavor that tastes slightly different from Danisco's and IDQ now uses both blue raspberry flavors in its system. Kosto, a DQOA supplier, submitted flavor samples to IDQ which IDQ found did not match either Danisco's or Coke's. Harris Cooper asked Glenn Lindsey if IDQ would sell Danisco flavors to DQOC's endorsed warehouses or to Kosto. Glenn Lindsey said he would inquire and later told Harris Cooper that IDQ declined. At one point IDQ considered approving Kosto flavors even if they did not match Danisco's, but DQOA noted its concern that stores would be disadvantaged by carrying flavors that consumers might recognize as different from expectations.

The upshot of both IDQ and DQOA's efforts were that neither could reproduce Danisco flavors. The fact that IDQ itself tried to replace Danisco and failed strongly suggests there is "no reasonable alternative" to the Danisco flavors. IDQ is then obligated under the Agreement to sell Danisco flavors to DQOC-endorsed warehouses at the same price and on the same terms that IDQ offers to its authorized warehouses.

2. <u>Manufactured Novelties</u>

The IDQ system offers a variety of novelty items that were originally assembled by the stores. Most of these items are now outsourced to an independent manufacturer, Wells Blue Bunny, who manufactures such novelty items as the Dilly Bars and the StarKiss. Wanting to offer stores competitive prices, DQOA began a search for companies who could manufacture novelties. DQOA found two interested companies, Fieldbrook Farms and Frostbite Brands. After signing a non-disclosure agreement and reviewing the specs,

Fieldbrook responded verbally to Josh Schmieg that it was not interested because it lacked sufficient capacity to go forward. Frostbite is a division of Dean Foods; Dean Foods supplies soft serve mix to IDQ. Frostbite presented a proposal to DQOA in early December 2002. Schmieg analyzed Frostbite's proposed pricing and concluded there was insufficient savings. Josh Schmieg wrote Terry Gray, Director of Foods Service Sales at Dean Foods/Frostbite Brands on December 11, 2002: "Management has reviewed your proposal of December 4, 2002 and the proposed pricing does not reach savings levels per item that would make the marketing of these products a Dairy Queen system success." [Respondents' Ex. 259] Frostbite sharpened its pencil and two weeks later submitted a revised proposal.[17] Frostbite's second proposal still failed to meet DQOA's pricing requirements.

Since §III.E.3 defines "reasonable alternative manufacturer" as one who (1)does not sell to IDQ, and (2)does not need to invest in major equipment, one question raised is, since Dean owns Frostbite, does it, for purposes of §III.E.3, "sell" to IDQ? A second perhaps related question is: if there is no or insufficient price-savings with an alternative manufacturer, does he cease to be a "reasonable alternative manufacturer" within the meaning of §II.E.3? Because the Arbitrator finds that Dean, the owner of Frostbite Brands, sells to IDQ, she does not address the second question.

[17] Frostbite's proposals of December 4 and 19, 2002 were tendered by Terry Gray, Director of Foods Service Sales for Dean Foods Southeast Region. The proposals were tendered on Dean letterhead.

4. **The Ultimate Box**

John Henry has spent 45 years in the paper box manufacturing business, 33 of those years with an IDQ supplier, International Paper. He now brokers for Paris Packaging a supplier of packaging to the food service industry. Paris Packaging currently sells to DQOC warehouses.

IDQ packages its Ultimate Sandwich in a Microflute box. Desiring to supply an alternative box to DQOC-endorsed warehouses, in Fall 2001 Henry began searching for Microflute. Paris Packaging first proposed to substitute a .014 SBS box as a functional equivalent that would perform as well as Microflute. [Claimants' Ex. 40] IDQ rejected the request on October 12, 2001. [Respondents' Ex. 141] Henry then contacted some twelve companies. None of the companies Henry contacted could supply Microflute and every contact lead him back to Burrows Paper Corp. as the single major supplier who could both manufacture and print on Microflute. Burrows supplied IDQ and also supplied the single largest user of Microflute in the food industry, McDonald's, to whom Burrows dedicated 80% of its plant capacity. Henry did find Ample Packaging in Ohio who had an agreement with Burrows to make Amples's packaging and print Ample's logo on it. Henry found that Dopaco, suggested by Mike Rinke in his letter of December 28, 2001 [Respondents' Ex. 147], had closed its plant.

On January 24, 2002, Mike Rinke next suggested Bell Incorporated of Sioux Falls, SD as a potential reasonable alternative manufacturer [Claimants' Ex. 45]; in response, Henry

contacted Bell who had the capability to pre-form and nest Microflute, but could not print it. Bell is in fact included on a list of companies Henry contacted. Harris Cooper enclosed this list in his letter to Glenn Lindsey on November 28, 2001. [Claimants' Ex. 41; Respondents' Ex. 144] Henry finally called Michael Hickey at Perseco, who does the buying for McDonald's, who told him that he knew of no one besides Burrows who did Microflute. Henry also contacted Smurfit- Stone. Henry did not testify that he contacted Arvco Containers, referred to by Mike Rinke as an alternative source in his letter of December 28, 2001. Glenn Lindsey, however, testified that he was not aware of any company in the U.S. besides Burrows that made Microflute. Ultimately, in March 2002, Cooper put on hold talks he had begun with a potential reasonable alternative[18] suggested by Mike Rinke in his December 28 letter to wait to see if IDQ was going to market a Bistro Burger and drop the Ultimate Box [Respondents' Ex.209].

Paris Packaging, through Cooper, originally asked for standards and specs on a variety of different trays, boxes and clamshells. [Letter of March 5, 2001; Respondents' Ex.134.] IDQ ultimately approved all but the Ultimate Box. As to the Ultimate Box, the Agreement provides: "If a disagreement arises…as to whether there exists a 'reasonable alternative manufacturer or processor' for a particular Product…DQOA/DQOC shall

[18] The parties are in disagreement whether Henry ever contacted Innovative Packaging. Claimants' claim that John Henry did contact Innovative Packaging; Respondents assert otherwise and in fact believe that Innovative Packaging was the "potential reasonable alternative" referred to by Harris Cooper. Cooper's letter of November 28, 2001 encloses "[a] list of various companies and contacts…All have indicated that they do not have the capability to manufacture the "Ultimate Box" to the IDQ specifications." [Respondents' Ex. 144] Innovative Packaging is not on the contact list. The Arbitrator has reviewed her extensive notes of John Henry's testimony and finds no reference to Innovative Packaging. On direct examination, after referring to Claimants' Ex. 41 through 45, and in particular to the list of companies he contacted [list attached to letter of 12/28/01, Claimants' Ex. 41] John Henry testified that he stopped looking for an alternative source of Microflute as no one was aware of anyone who operated in this specialty niche business besides Burrows.

designate, in writing, the steps…that the DQOA/DQOC representatives have taken to locate a 'reasonable alternative manufacturer or processor,' including the names…that have been contacted, the approximate date(s) of contact(s) and the results…" Agreement, §II.5.a. IDQ may then, within 20 business days "…designate, in writing: (1) their position…and the names and addresses of manufacturers or processors that might be potential 'reasonable alternative manufacturers or processors' of the Product." Agreement III.5.b. And then, if after the exchange of written designations the parties are still in disagreement, DQOA may elect to submit the dispute for resolution through binding arbitration. Nothing in the Agreement suggests DQOA need search further.[19] Although the evidence might suggest, as interpreted by IDQ, that Harris Cooper might have been in contact with Innovative Packaging, the Arbitrator weighs this suggestion against the more powerful admission against interest by Glenn Lindsey, IDQ's R & D Director, that he was not aware of any company besides Burrows who manufactured Microflute. The Agreement, §III.E.1, suggests once DQOA has certified there is not a reasonable manufacturer or processor, IDQ shall, "**after determining…that there is not a 'reasonable alternative manufacturer or processor**'" (emphasis added), either approve a functional equivalent or sell direct to DQOC-endorsed warehouses at the same price and on the same terms that the Product is sold to IDQ-authorized warehouses. The parties have mooted the argument by their subsequent behavior: rather than asking for arbitration and putting the burden of proof on IDQ, DQOC, on its part, continued to attempt to find an alternative source [Respondents' Ex.144] and IDQ, on its part,

[19] IDQ interprets DQOA's obligation at this point as having to contact IDQ-suggested alternative manufacturers. [IDQ /ADQ Post Hearing Memorandum, p. 31] As a practical and legal burden-of-proof or burden-of-going-forward matter this may be so. The Agreement, however, provides that once IDQ has designated potential product sources, if DQOA still disagrees, the matter is ripe for arbitration.

discontinued the Ultimate Box. In November 2001 the matter was at issue and DQOA might have appropriately and timely presented the issue for arbitral decision.

D. Development of New Products and Limited Time Offers

On October 17, 2002 Harris Cooper wrote Glenn Lindsay for summary specifications for new Blizzard® flavors for 2003. The Franchisee Advisory Council met November 12-14, 2002 and apparently approved the Keebler® Fudge Stripe cookie branded product as a “new product” flavor for April 2003. Jerry Rizer’s November 15 notes to Cooper of the meeting indicate “LTO – Keebler Fudge Stripe” and the comment that Keebler will be giving franchisees coupons to hand out for their cookies. Elizabeth Matzen wrote Harris Cooper on November 25 with this information, acknowledging Lindsey’s receipt of Cooper’s October request and telling Cooper to expect a more comprehensive response on the plans for the 2003 flavors. [Respondents’ Ex. 104] Harris faxed his October 17 letter, marked “2nd REQUEST”, to Lindsey on December 2. [Claimants’ Ex. 48.] On December 4, Lindsey responded with the 2003 schedule for Blizzard® of the month calling for chopped Keebler Fudge Stripe Cookies for April 2003. On December 12, 2002 Cooper asked for summary specs for *non-branded* products [Respondents’ Ex.106] and on January 21, 2003, Cooper wrote Lindsey requesting standards and specs for any special grinds of the Keebler® product. [Respondents’ Ex. 107] On January 30, Lindsey provided the summary specs for the Keebler® Fudge Stripe Cookie grind, the chosen flavor for April 2003.

Tim Tarrier, president of Tarrier Foods Corp., testified that Josh Schmieg contacted him at the end of January 2003 to work on a new product, the Keebler® Fudge Stripe cookie that would run as a new product in an LTO for a couple of months. Tarrier told Schmieg that he would need the specs and a sample from IDQ so that he could prepare a sample for approval. In February[20] Tarrier contacted Keebler for pricing and availability; in March, Gregg James, National Account Manager for Keebler, told Tim Tarrier that Tarrier Foods would have to buy full truckloads, but that since IDQ was buying in huge quantity, no product would be available until the end of April. Apologizing for a delayed response, Keebler quoted Tarrier a price on April 11 with next production scheduled for the week of April 28. [Respondents' Ex. 108A.] Tarrier said that he was willing to buy a truckload, but that timing was a problem since the LTO promotion began in April.

Claimants argue that Respondents purposefully purchased Keebler's entire supply of its requirements for the April 2003 promotion because they had the product specs long before Claimants. While conceding that IDQ developed its specs before providing them to DQOA, the testimony is not determinative on the issue. In early December 2002, Glenn Lindsey notified Harris Cooper that Keebler's *branded* product would be included in the April 2003 Blizzard promotion. Harris Cooper wrote back asking for summary specs for *non-branded* products. Not until January 21, 2003 did DQOA ask for special grinds of the Keebler Cookie. Almost seven weeks had elapsed. The Arbitrator cannot

[20] Witness testimony was not transcribed. The Arbitrator and counsel for the parties took copious notes. Respondents recall Tarrier responding to an Arbitrator's question that he first contacted Kraft/Nabisco in March. The Arbitrator's notes – approximately 207 handwritten legal pages – reflect that on re-direct examination Tarrier responded that he first called Gregg James in February 2003.

determine if, had DQOA notified Tarrier earlier and had Tarrier placed its order earlier, supplies would have been available to Tarrier before April.

IV. Breaches of the Agreement: The Faailure to Act in Good Faith

The Agreement requires IDQ to "exercise good faith and act reasonably in applying the product approval procedures…" §III.C.1a. As a matter of course, IDQ requires any proposed alternative supplier to sign a non-disclosure agreement before product specifications are released. DQOA apparently requires Lyons Magnus (for many years an IDQ toppings supplier, still the IDQ supplier to Texas stores, and currently the DQOC-endorsed supplier of approved toppings), to sign a new non-disclosure agreement for each new product approval request even though, according to Harris Cooper, a master non-disclosure agreement is already on file. Only after Lyons Magnus signs each non-disclosure agreement will IDQ then send requested product specifications. [IDQ Ex. 162.]

The parties need not fight about this point. The Agreement deals specifically with non-disclosure agreements. Section III.C.1.e requires Respondents to provide Claimants with non-disclosure agreements which Claimants can provide directly to manufacturers. Claimants need not wait for IDQ to send out a non-disclosure agreement. With sufficient forms on hand, DQOA can control the timing of delivery of these agreements.[21] Inferentially, IDQ has an obligation to keep DQOA supplied with the most current forms as amended from time to time. Section III.F.2 appears also to contemplate DQOA's

[21] The Arbitrator notes that §III.C.1.e appears to contradict this protocol. That section directs IDQ to "send a proposed manufacturer or processor a non-disclosure agreement." Reading the Agreement provisions together, DQOA may either request IDQ to send a non-disclosure agreement or send it itself.

control of the non-disclosure signing process. Addressing new product recommendations by the Franchise Advisory Council, §II.F.2 contemplates the DQOA submitting information regarding an alternative manufacturer "together with the non-disclosure agreement…"

V. <u>Summary and Concluding Remarks on LTOs and Branded Products</u>

IDQ views this arbitration as one to enforce the Agreement. The DQOA also beseeches the Arbitrator to "require Respondents to honor the Dairy Queen franchisee's contractual rights…" Underscoring the request of both sides to enforce the Agreement are lurking fears. IDQ believes that the DQOA is using this arbitration "for its own political and economic ends", to "villanize IDQ" and "to rally franchisees with vitriolic rhetoric."[22] IDQ is stung by what it reads as jeremiads in Claimants' trade publication, *The Bottom Line,* and by Jerry Rizer's testimony to Congress [IDQ Ex.288] DQOA worries that IDQ has not performed the Agreement in good faith and instead "manipulate[s] the product approval, sourcing and distribution process to their benefit", thereby breaching the Agreement.[23] IDQ accuses Claimants of "lack of remorse" and fears that no ruling "will truly cause claimants to mend their ways." IDQ hopes for a "firm ruling which will lead claimants to think twice before continuing their demagogic ways."[24]

The franchisor-franchisee relationship is, by definition, symbiotic. It is a perfect example of market interdependence. The franchisor depends for its continued existence and

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[22] IDQ/ADQ Post-Hearing Memorandum, pp. 2, 6.
[23] Claimants' Post Arbitration Brief, p.1.
[24] IDQ/ADQ Reply Memorandum, p.2.

profits on its franchisees. The franchisees' identity springs from the franchisor; the goodwill of both franchisor and franchisees turn in large part on the innovations of the franchisor and the resulting hoped-for market share dominance. There is also an inherent, and in this instance destructive, tension in the relationship because the franchisor competes with extant and potential suppliers of approved product for sales to the franchisees. As IDQ properly views it, "IDQ and claimants are competitors when it comes to the distribution of product."[25] The same can be said for product sourcing.

The Arbitrator will not act as a scourge to either party. Although both sides might wish it, it is in the interest of neither to be taken to the woodshed. And the Arbitrator admonishes both not to wear the arbitration Award as a badge of victory. That having been said, the Arbitrator seeks to achieve two goals in this Award: an interpretation of the Agreement such that the parties can operate under its terms with greater understanding and less friction; and the ability of the parties to communicate with greater ease and less misgiving. As to the first goal, the Arbitrator's duty is to give meaning to the Agreement by making its operational terms precise, not to hand either party a bully pulpit. Mistrust runs exceedingly high between the parties; if this were a civil marriage, both parties would be filing for divorce on grounds of irreconcilable differences or emotional cruelty. But this marriage is commercial; it has a market place reality and dissolution would mean the liquidation of many businesses and business dreams for family-run franchisees and the end of a half-century long American success story.

[25] IDQ/ADQ Reply Memorandum, p. 28.

DQOA complains of multiple violations of the Agreement and believes that IDQ's desire to keep its franchisees alive, but barely profitable, motivate its actions. DQOA believes IDQ only grudgingly allows competition and then with a maximum of impediment. On its part, IDQ complains that DQOA does not respect IDQ and engages in hyperbole and histrionic accusation in DQOA's newsletter, *The Bottom Line*, and elsewhere. The parties in §III.M "agree to demonstrate mutual respect for one another and to cooperate in good faith with one another for the advancement and improvement of the 'Dairy Queen' system." While not limiting the scope of their commitment, the parties do agree that it includes such things as communications, the exchange of information, and refraining from interference. Certainly the language headlining the May 2002 edition of *The Bottom Line* – "BUFFET BULLIES DAIRY QUEEN FRANCHISEES" – is worded to grab attention. The front page article assails "Warren Buffet, self-made billionaire investor" (whose company Berkshire Hathaway owns IDQ) as the "greatest competitive threat" to the franchisees. The article expresses DQOA's fear that new DQ Grill & Chill franchise stores are encroaching on existing franchise territories and bemoans the lack of federal legislation to protect existing stores. In part, this was the gist of Jerry Rizer's testimony to Congress. The tone of the newsletter article is excited and emotional, and, yes, it criticizes IDQ. Is it "respectful?" IDQ will certainly not read it dispassionately or without being angered. Are the words chosen intended to goad IDQ? Probably. Might IDQ not feel kindly towards IDQ after reading such articles? We know the answer. But to order respect if that means requiring a party to curb his speech is something this Arbitrator does not think the parties contemplated in their Agreement. The Arbitrator, mindful that she "may not under any circumstances:…(3)make any award that

extends…any lawful term of this Settlement Agreement”,[26]is unwilling to make an award that arguably infringes First Amendment freedoms. The goading tone of the article is symptomatic of the problem. To order DQOA to “demonstrate respect” is like ordering a feverish patient to produce a normal temperature. You can pack the patient in ice and reduce the fever; ultimately the causative, not the presenting, problem needs be addressed.

A further note: Claimants ask the Arbitrator to order Respondents to sell the DQOC-endorsed warehouses manufactured novelties and LTO products which DQOC-endorsed manufacturers are unable to produce in time to participate in an LTO at the same price and on the same terms as IDQ-authorized warehouses. This Award addresses certain products in dispute. To issue a general order as to all future manufactured novelties and LTO products would be to simply restate the terms of the Agreement. Respondents’ in turn request a finding that §III.E of the Agreement does not apply to the majority of LTOs which are third-party branded products. While that may be statistically true, Respondents’ request begs the question of exactly what a third-party branded product is, and, in the context of this hearing, is a branded-product still a branded product when used in an altered, *eg.* broken, crumbled, crushed or ground state?

Referring to the Arbitrator’s Order and Opinion of January 16, 2004, a “brand” is “a trademark or distinctive name identifying a product or a manufacturer…to show quality

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[26] Agreement, §III.O.2.

of contents…”[27] A trademark or brand connotes a measure of uniformity and quality in the public mind which attaches to the usual form in which the product is presented to the consumer. So, whereas a whole Oreo® cookie or a whole Keebler® cookie is exempted from “reasonable alternative manufacturer or processor” by §III.E.3, the altered *form* of that cookie is not. DQOA may not seek an alternative manufacturer of a crème-filled chocolate sandwich cookie if IDQ specifies Nabisco® Oreo, but if the Product is to be used in an altered state which does not change its taste, texture, chemical composition, ability to identify, and does not add or subtract any ingredients, DQOA may seek an alternative processor, such as Tarrier, to replicate IDQ’s specified grind.[28]

This Award resolves all claims submitted by the parties for decision in this proceeding.

Dated: April 2, 2004

Judith P. Meyer
Standing Arbitrator

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[27] American Heritage Dictionary of the English Language, 4th Ed.; Webster’s Revised Unabridged Dictionary, 1996.

[28] There was testimony at the hearing that Oreo® grinds its own product and offers it for sale. If Nabisco is the sole source for this *ground* product, then §III.E.1.b might apply.