

THE CITY OF NEW YORK
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October 30, 2003

Hon. Michael A. Cardozo
Corporation Counsel
New York City Law Department
100 Church Street
New York, N.Y. 10007

Dear Mr. Cardozo:

I am in receipt of your October 14, 2003 response to my October 2, 2003 letter to Chancellor Klein regarding the Department of Education's and the City's proposed contracts with Snapple. I am also in receipt of your second letter, dated October 17, 2003, which included copies of DoE's interim agreements with Snapple and Octagon and the Letter of Intent between the NYC Marketing Development Corp and Snapple. Your second letter, however, did not include all of the documentation I had requested of the Chancellor, in particular, information regarding the integrity of the bidding process.

Upon my staff's review of the information you provided, as well as the information my office obtained independently, it appears that:

- The Snapple agreements were awarded without open and fair competition;
- There are clear conflict-of-interest concerns with respect to Octagon, Cadbury and Interpublic Group (an affiliate of Cadbury and Octagon), and a potential conflict with respect to NYC Marketing.

Based on these serious breaches of the fundamental aspects of standard public bidding and the apparent and potential conflicts of interests, the City should cancel the proposed Snapple agreements.

The Snapple agreements.

The DoE Agreement

The DoE interim agreement provisionally gives to Snapple and its affiliates, which include Cadbury-Schweppes, a five-year license to be the exclusive provider of fruit juice and water to NYC school vending machines. It also gives to Snapple and its affiliates the exclusive rights to provide any of its cold beverages to faculty/employee lounges. The agreement contemplates that Snapple will sell to the school children a minimum of 30 million bottles of juice and water per year (150 million bottles over the five-year term of the agreement).

In return, Snapple will pay to the City approximately \$3 million per year to support physical education and sports in the schools. Snapple will also pay thirty percent of the price of every bottle sold, currently set at \$1.00, with a guaranteed minimum amount of \$25.2 million over the five-year period. No financial details were provided in the license agreement with respect to the faculty/employee lounges.

My staff has been provided with copies of a number of PowerPoint presentations made by Octagon, DoE's marketing agent, to potential bidders. I am enclosing a copy of the presentation made to Apple and Eve, LLC for your information. Copies of the presentation made to Pepsico and VeryFine are also available.

Although not in the Agreement but according to the presentation made to bidders by DoE's marketing firm, Octagon, Snapple will not only receive the profits from the sale of its products to 1.1 million students and 150,000 faculty and employees, but will also be granted the exclusive rights to advertise in 500,000 student day-planners, place its name and logo on basketball backboards, gymnasiums, cafeterias, athletic fields and various general use facilities. Additional opportunities for Snapple to market its brand identity will be provided through corporate sponsorship events and patches on student athletic uniforms.

NYC Agreement

The Letter of Intent between NYC Marketing and Snapple provides that Snapple and its affiliates will be awarded a five-year license to be the exclusive seller of water, iced teas and chocolate drinks City-wide. The Letter of Intent also provides for the potential to award Snapple's parent, Cadbury-Schweppes, the exclusive rights to sell City-wide its entire roster of products. Under the Letter of Intent, the City is required to guarantee that

Snapple sell a minimum of 24,024,000 bottles a year (120,120,000 bottles of its drinks over five years).

In return, Snapple will fund \$6 million per year in marketing initiatives, plus "supplemental marketing value" of \$12 million per year to promote the City. Examples of the City promotions that would count toward the \$12 million include putting the City logo on Snapple

trucks, using the City as a backdrop in Snapple advertising, and other marketing initiatives in lieu of additional payments to the City. In addition, Snapple will pay NYC Marketing thirty percent of the price of every bottle sold, which is \$7.2 million based on their guaranteed sales of \$24,024,000 per year. To date, we have not seen the agreement between NYC Marketing and the City of New York. Until we see this agreement we will not know what portion, if any, of the \$7.2 million will accrue to the City.

The Lack of Open and Fair Competition.

As I stated in my earlier letter, the DoE's marketing firm, Octagon, failed to provide bid documents that would have allowed all firms to know exactly what it was that they were to bid on or how they were to be rated. This is most evident by the fact that one firm reported to my office that it was told the bid was limited to only fruit juice, and not both fruit juice and water. Another indicated that it was encouraged to include snacks in its bid. That is a violation of standard public bidding practices and creates an un-level playing field among bidders.

All firms that contacted my staff represented that they were expressly told not to bid on faculty/employee lounges, and they were not informed that City-wide marketing opportunities were also up for bid.

Two of the firms have provided information that indicates that their bids were equal to or better than Snapple's negotiated \$40.2 million Interim Agreement with the DoE, yet no negotiations took place with them. In fact, one bidder was told by Octagon that his initial bid was so "formidable" that Octagon was going to extend the bid deadline, as indeed they did, to allow "other companies to respond."

The failure to include the other vendors in the related City business contract and Faculty/Employee lounges is inherently one-sided. The profit and marketing potential to a vendor from the City-wide agreement with NYC Marketing is enormous and would have had a significant impact on any bids to the Department. Likewise, the potential rights to sell to 150,000 faculty members and employees would surely have also had an impact on the bids to a significant extent.

Further, it is inherently illogical to state that NYC Marketing used the DoE "competitive" process as the basis for the selection of Snapple to be the exclusive provider of beverages and the sponsor of the entire City of New York. As described in the Letter of Intent between Snapple and NYC Marketing, the City-wide agreement would be three times the size of the DoE agreement. For this reason alone, the contracts should be re-bid.

Conflict-of-Interest Issues

NYC Marketing and Snapple.

Joseph Perello, the City's Chief Marketing Officer, was previously the Vice-President for Marketing for the New York Yankees. During his tenure with the Yankees, Mr. Perello brought in Snapple as "The Official Iced Tea of the Yankees." As such, Snapple holds the exclusive rights to sell its iced tea drinks at the stadium and to routinely sponsors events, such as Snapple Night. Given the relationship that existed between Mr. Perello and Snapple prior to his engagement with the City, to avoid any appearance of favoritism, he should have recused himself from discussions with Snapple. At the very least, he should have requested an opinion from the Conflicts-of-Interest Board before he entered into discussions with Snapple.

Octagon and Cadbury.

I previously questioned the propriety of this entire process because, among other reasons, Octagon is also Cadbury's marketing agent. Both Snapple and Cadbury are owned by Cadbury-Schweppes. You replied that there were no conflict issues because different Octagon staff represent Cadbury's business overseas. While it is not clear why that would imply there was no conflict, I am concerned that you may not have been aware that the proposed City-wide agreement is, in reality, a contract with Cadbury's and Snapple's owner, Cadbury-Schweppes, and not just Snapple. This connection opens up a clear conflict-of-interest question regarding Octagon's client Cadbury. The Letter of Intent between NYC Marketing Development and Snapple states:

"NYC Marketing grants to Snapple and entities controlling, controlled by or under common control with Snapple . . . the exclusive rights to locate, maintain and operate vending machines in vending locations approved by the City of New York, . . ." (Emphasis added)

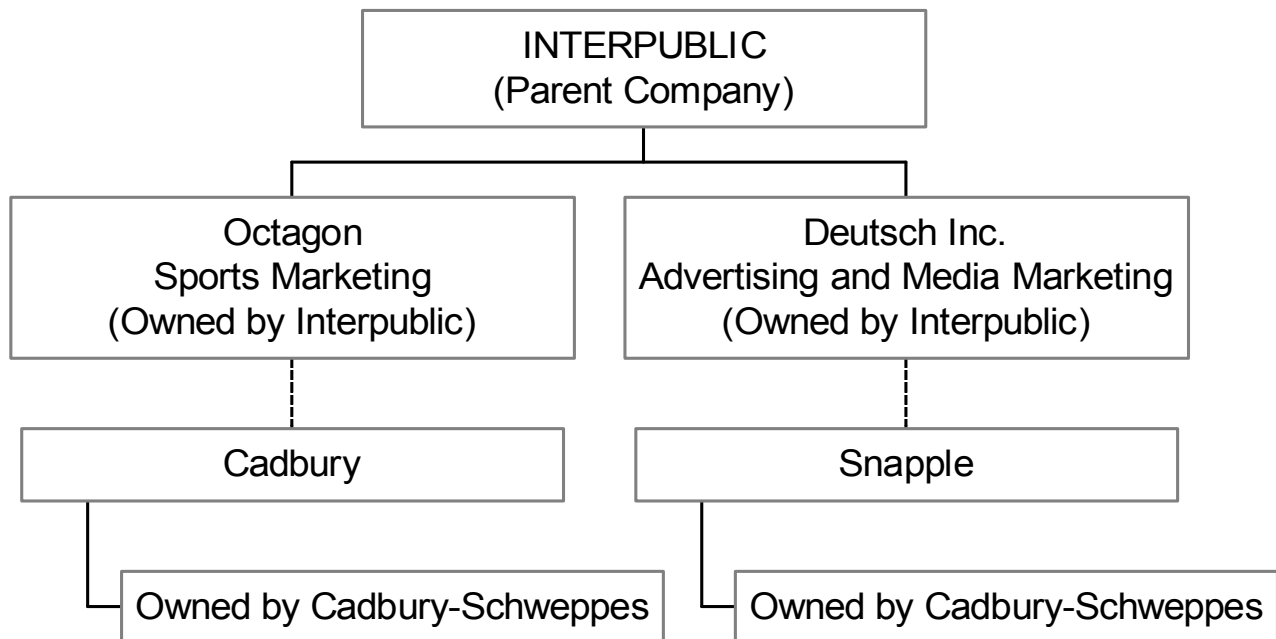
In 2002, Cadbury-Schweppes did over \$3 billion in sales in North America, of which, \$2.7 billion was for beverages and \$373 million was for confectionery products.

The Letter of Intent gives to Cadbury-Schweppes the rights to provide "water, iced teas, chocolate drinks and other mutually agreed [upon] products" throughout New York City. Cadbury-Schweppes controls Halls, Trident, Chicklets, Dentyne, Certs, Cadbury Chocolate products, Hawaiian Punch, Canada Dry, Dr. Pepper, 7-UP, RC Cola, Sunkist, Mott's Apple and Fruit Juice, and Snapple to name just a few of their products. Consequently, under the terms of the Letter of Intent, Cadbury-Schweppes could receive a virtual monopoly on City business without a trace of competition.

The scope of the proposed agreement between Snapple and NYC Marketing goes far beyond anything made public to date raising the question that the City may not have received as large an economic benefit as it should have. The fact that the scope of the deal was significantly expanded without complete and consistent information to all potential bidders is extremely troubling.

Octagon and Snapple's advertising and marketing agency are owned by the same company.

Compounding the problems associated with Mr. Perello's prior relationship with Snapple, and Octagon's relationship with Cadbury, is the previously undisclosed affiliation between Octagon and Snapple's advertising and marketing agency, Deutsch Inc. Both Octagon and Deutsch are owned by the same company, the Interpublic Group (Interpublic). (See chart that follows.) Deutsch has been Snapple's marketing and advertising agency since 1997. This fact compounds - exponentially - the potential for favoritism in a process that should have been, but was not, open, fair and competitive.



I would also like to address the selection of Octagon as DoE's marketing agent. In your October 14th letter, you stated that Octagon was chosen through a competitive process by the Board of Education. That is not the case. In late 2001, the then Board of Education issued a Request for Proposals. The firm that was ultimately recommended for contract award was Growth Through Sports Marketing, LLC (GSM). My staff has been informed that GSM was formed by Bober Associates, Edelman, and New Tech Capital for the sole purpose of bidding on the Board's marketing contract, although there is no record that GSM ever registered with the State as a LLC and was, thus, not legally eligible to do business in New York State. On May 15, 2002, at its regularly scheduled meeting, the contract was withdrawn from consideration by the Board. There is no record that the Board ever voted in favor of the contract.

In August 2002, Octagon purchased Bober Associates. Mr. David Bober is now employed by Octagon and, in fact, was the contact between Octagon and the firms who attempted to bid for the Department's contract. Consequently, Octagon itself was not chosen through a competitive process, but instead received its contract solely by virtue of acquiring one of the three firms that had previously

submitted a joint proposal to the former Board of Education. As evidenced by the June 23, 2003 Interim Agreement between Octagon and the BoE, no formal contract between the parties has been executed.

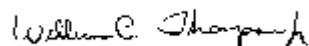
I am aware that the Board of Education previously did not present its concessions to the Franchise and Concession Review Committee (FCRC). Nevertheless, now that the governing body, the Board of Education, has been dissolved, there should be, but is not, sufficient oversight nor a public process whereby important matters such as those described above can be heard. The fact that the Department of Education, a \$12 billion a year entity, has the ability to enter into the contract outlined above without public scrutiny raises serious questions about the Department's governance controls and accountability.

New York City's entrance into corporate sponsorship is an unprecedented opportunity and the process by which the sponsor firms are chosen should be a model for all cities to emulate. Unfortunately, given the failure of both the DoE and NYC Marketing to follow

the most basic tenets of public bidding, the DoE should cancel both its marketing and beverage agreements, and the City should begin a truly competitive process that will ensure that we are entering into the best deal on behalf of the people of the City of New York.

I look forward to learning your views on this matter.

Very truly yours,



William C. Thompson, Jr.

cc: Chancellor Joel Klein