

## How to write a development agreement: a case study of City of Albany v. PepsiCo

### A case study of City of Albany v. PepsiCo

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PepsiCo Inc. recently settled, for more than \$25 million, a lawsuit that stemmed from a development agreement between a PepsiCo subsidiary and several government entities, including the city of Albany. In February 2009, Albany filed claims in Linn County Circuit Court after PepsiCo reneged on promises to build a \$250 million Gatorade manufacturing facility, which was to provide at least 250 local jobs. The terms of the development agreement provide a case study in good lawyering by the city attorney and in how to deal with the unexpected.

PepsiCo in 2006 began identifying communities where it could build a large facility to accommodate expected double-digit sales growth for Gatorade. Albany met all of PepsiCo's requirements for a site: hundreds of acres of available land zoned for industrial use, transportation efficiencies along Interstate 5, rail access, millions of gallons of water available every day, state-of-the-art sewer systems, and local labor.

PepsiCo said the economic benefits of the project for local and regional economies would range from \$5 billion to \$7 billion - and more if the plant capacity were doubled, as planned, over the course of just 10 years.

Albany was uniquely positioned to win this contract because it has an abundance of water from redundant sources. It had been planning for such an opportunity. PepsiCo tied up the land it would need, and proceeded to negotiate the development agreement.

Albany agreed to tax-abatement and system development charge concessions, and committed to construct infrastructure improvements totaling more than \$17 million. These concessions consumed much of the negotiations and contract drafting. To a lesser degree, the parties documented PepsiCo's promise that it would bring hundreds of family-wage jobs to the community, coupled with fees that would be due if PepsiCo failed to meet certain minimums.

What went unstated was any specificity about the economic advantages to any tax base, or any specific promise about how much water PepsiCo would purchase. Those expectations were real and mutual, but undefined when City Council approved the deal in October 2006.

What happened next was unanticipated. Double-digit sales growth for Gatorade in the U.S. dried up. PepsiCo decided that its most economically efficient option was to breach the development

agreement. Within six months of inking the deal with Albany, PepsiCo negotiated an amendment for up to three years of delay and agreed to pay Albany more than \$700,000 per year for losses associated with water and sewer revenues. Then, in November 2008, PepsiCo announced that it would abandon the Albany project.

The contracting parties never imagined that PepsiCo would fail to perform. In fact, PepsiCo representatives had warned the city during earlier negotiations that the contract presented unlimited exposure to damages if the city's infrastructure obligations were not completed on schedule. PepsiCo's warnings resulted in a contract devoid of any provision that would have protected PepsiCo (or Albany) in the case of breach. The development agreement had no limitation of liability clause and no arbitration clause, and the venue for any legal claim was set for Linn County.

The city had been led to believe that while market conditions dictated a delay in construction, PepsiCo remained committed to fulfilling its obligations under the development agreement.

On Nov. 20, 2008, however, PepsiCo scheduled a meeting to announce its decision to breach. PepsiCo knew that a corporate decision had already been made to abandon the Albany project, but that information was not communicated to the city in advance of the meeting. While PepsiCo was apologetic, and expressed the position that all that was lawfully owed to the city was the \$3 million of out-of-pocket cost incurred by the city up to that time, PepsiCo offered by the end of the meeting to pay as much as \$10 million in complete settlement of all city claims. PepsiCo made it known that this offer would expire by Dec. 31 unless accepted by that time.

While PepsiCo's offer would have compensated the city for its actual out-of-pocket expenditures, Albany City Council decided that the offer did not compensate the city for the loss of the predictable revenues anticipated if PepsiCo had honored its contract.

Albany engaged my firm, Markowitz, Herbold, Glade & Mehlhaf PC, to advise it concerning its contractual rights and to attempt to negotiate adequate compensation to the city without entering litigation. We offered nonbinding mediation in an attempt to resolve the dispute without litigation. PepsiCo representatives rebuffed our offer and reiterated their demand that the city accept their offer of \$10 million or proceed to litigation.

Litigation followed in February 2009. Albany asked the court for pretrial rulings that PepsiCo was liable for breaching the contract, that PepsiCo was liable for the fees described in certain contract provisions, and that these fees were not Albany's sole and exclusive damages. The contract was clear in this regard, and the court ruled for Albany as a matter of law.

Additionally, the court granted Albany's request that PepsiCo be ordered to give up documents that it had refused to provide, including economic analyses of similar Gatorade plants, water and sewer volume data from other plants, business appraisals, and strategic marketing data for its

Gatorade and Propel products. As the litigation swung in the city's favor, PepsiCo finally agreed to formal mediation, which resulted in a settlement to the city valued at more than \$25 million.

Local governments can learn from what could have otherwise been a disastrous result.

Take a long-term view to planning for economic development. It may not happen this year, this decade, or at any time this generation, but planning ahead will put future decision makers in position to capitalize.

Don't be cowed by a Fortune 500 company into giving everything and taking nothing. If a city has what the company wants, such as water and land, trust that its negotiating team will not undermine management's decision by negotiating unfairly.

Make sure the company backs up its promises, particularly the parties' expectations of economic benefits, in writing. Absent a limitation of liability clause, those expectations will be the cornerstone of your legal claims for damages in the case of breach.

Finally, don't be afraid to ask for clauses otherwise not expected. For example, if the Albany city attorney had not negotiated for a clause setting Linn County as the exclusive place to litigate any dispute, we probably would have found ourselves fighting this battle in New York.

At the conclusion of the mediation process, both sides shook hands and appeared satisfied that a fair outcome had been achieved. The city thanked PepsiCo for honoring its obligations to the city, and both sides expressed hope that a new buyer can be found for the site.

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