

Court File No.: 07-CV-333934CP

**ONTARIO  
SUPERIOR COURT OF JUSTICE**

**BETWEEN:**

**LANDSBRIDGE AUTO CORP. and  
405341 ONTARIO LIMITED**

Plaintiffs

– and –

**MIDAS CANADA INC. and  
MIDAS INTERNATIONAL CORPORATION**

Defendants

*Proceedings under the Class Proceedings Act, 1992*

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**STATEMENT OF DEFENCE**

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1. Midas Canada Inc. ("Midas Canada") and Midas International Corporation ("Midas International") (collectively, "Midas") admit the allegations contained in paragraphs 2-4, 13, 32, and 62 of the statement of claim (the "Claim").
2. Midas denies the allegations contained in paragraphs 5-12, 14-31, 33-61, and 63-85 of the Claim.

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### **Overview**

3. Sections 3.2(a) and 3.2(b) of the Midas Franchise and Trademark Agreement (the "Franchise Agreement") between Midas, the Plaintiffs, and the putative class provides that Midas can set the prices at which it sells products to franchisees, change product prices at any time without notice, and stop selling products if it believes such sales are unprofitable or undesirable.

4. The Franchise Agreement also contains, in section 10.9, an "entire agreement" clause that specifically excludes any "representations, undertakings, agreements, terms or conditions" not explicitly referred to.

5. Taken together, these provisions preclude the claims or causes of action alleged in the Claim against Midas relating to changes in the supply chain, the prices at which products were sold by Midas to the putative class, and the transition to provision of products by a third-party supplier, Uni-Select Inc. ("Uni-Select").

6. Furthermore, nothing in the Franchise Agreement prevents Midas from funding its warranty program through supplier rebates. The Charter document referred to in the Claim has no contractual force, but even the Charter expressly permits payment of rebates for funding warranty programs.

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### **Midas and the Franchise System**

7. Midas Canada carries on business from offices located at Markham, Ontario. It is the franchisor of the Midas franchise system in Canada.

8. Midas International carries on business from offices located at Itasca, Illinois. It is the franchisor of the Midas franchise system in the United States of America. The plaintiffs and the putative class have no contractual relationship with Midas International.

9. Since at least 1961, Midas Canada or its predecessors, itself and through its licensed affiliates and franchisees, has carried on the business of automotive service and repair, including exhaust, brakes, steering, and maintenance services and, until 2004, also distributed automotive products in Canada.

10. The Franchise Agreement governs the relationship between Midas Canada and each of the plaintiffs. The Franchise Agreement establishes the terms and conditions upon which franchisees are licensed to utilize a number of Midas' trademarks, the goodwill associated with those trademarks, and other components of the Midas franchise system. One significant feature of the franchise system is the lifetime warranty provided on select products designated "genuine Midas products". The Franchise Agreement is also not onerous on franchisees. For example, under the Franchise Agreement, franchisees have the contractual right to terminate their Franchise Agreements on 30 days notice and none of the Franchise Agreements contains a post-termination non-competition provision.

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**Plaintiffs**

**(a) 405341 Ontario Limited**

11. The Franchise Agreement between 405341 Ontario Limited ("405341") and Midas Canada is dated August 1, 1989 and relates to a Midas shop located in Concord, Ontario.

12. 405341 previously operated a Midas shop in Weston, Ontario pursuant to a Franchise Agreement dated October 6, 1981. 405341 provided Midas with a full and final release when it assigned that Franchise Agreement and 405341 cannot therefore assert any claim in respect of the 1981 Franchise Agreement, or any representation about a 14.5% discount that is alleged to have been made by Midas in 1980-81.

**(b) Landsbridge Auto Corp.**

13. Landsbridge Auto Corp. ("Landsbridge") became a franchisee on August 1, 2004.

14. Five weeks before executing the Franchise Agreement, Midas provided Landsbridge with a disclosure document that disclosed, among other things, how the Midas system worked, how the supply agreement with Uni-Select worked, and that Midas received a rebate from Uni-Select to fund its warranty obligations.

15. In the last two years, Landsbridge has failed to pay monies owing to Midas under the Franchise Agreement on approximately eighteen (18) different occasions, resulting in

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approximately six (6) defaults of Landsbridge's Franchise Agreement or its sublease with Midas. After Landsbridge agreed to pay the monies owing over time, Landsbridge stopped payment on a cheque to Midas resulting in the termination of its Franchise Agreement by notice dated March 6, 2008.

#### **The 1981 Franchise Agreement and the 14.5% Discount**

16. In 1980-81, Midas introduced a new form of franchise agreement (the "1981 Franchise Agreement"). The plaintiffs admit in paragraph 16 of the Claim that the 1981 Franchise Agreement was negotiated by Midas and a franchisee association known as the Canadian Midas Dealers Association (the "CMDA").

17. The 1981 Franchise Agreement required franchisees to pay a royalty of 10% (the royalty had previously been 5%) but also granted them a right to renew the Franchise Agreement at the end of the initial term, a contractual right that franchisees had previously not enjoyed. The right to renew was extremely valuable to franchisees because it allowed them to remain in the system over the long term, and provided franchisees interested in selling their franchise with a more marketable asset. Furthermore, Midas also agreed to apply one-half of the 10% royalty toward advertising (which would benefit all Canadian franchisees).

18. When the 1981 Franchise Agreement was unveiled, Midas stated that it would discount the price of its products by 14.5% to those franchisees who entered into the new agreement.

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19. The 14.5% discount was not, however, in the Franchise Agreement and was not a contractual obligation of Midas. In fact, the 1981 Franchise Agreement expressly provided that Midas had the right to set and change prices of its products from time to time (s. 3.2(b) of the 1981 Franchise Agreement) and it also contained an entire agreement clause (s. 10.9 of the 1981 Franchise Agreement).

20. The pertinent part of section 3.2(b), the provision dealing with price and supply, provides:

3.2(b) The prices, delivery terms, terms of payment, and other terms relating to the sale of such products by Midas shall be as prescribed by Midas from time to time, and shall be subject to change by Midas without prior notice at any time.

21. The pertinent part of s 10.9, the entire agreement clause, provides:

10.9 This Agreement [...] constitutes and contains the entire agreement and understanding of the parties with respect to the subject matter hereof [...]. There are no representations, undertakings, agreements, terms or conditions not contained or referred to herein [...]. This Agreement supersedes and extinguishes any prior written agreement between the parties or any of them relating to the operation of the Shop [...].

22. Between 1981 and late 2003 (when Midas began to wind down its manufacturing and distribution operations), Midas exercised its contractual right under the Franchise Agreement to change the prices of its products many times. The price increases, however, always preserved

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preferential pricing - in the form of a 14.5% discount - for franchisees that had entered into the 1981 Franchise Agreement.

23. In late 2003, when Midas began winding down its manufacturing and distribution operations, any obligation that Midas had (which Midas denies) to offer a 14.5% discount came to an end.

24. From spring/summer 1981 through August, 2001, Midas Canada described the prices of products it distributed on its price lists and invoices using the terms "net" and "net net". The "net net" price was 14.5% less than the "net" price.

25. In August 2001, Midas Canada changed its computer system and began issuing price lists and invoices to franchisees showing the same figure previously labelled the "net net" price but referring to it as the "net" price. While the terminology on the invoice changed from "net net" to "net", the 14.5% discount on products distributed by Midas remained as long as Midas distributed products. Midas explained the change in terminology in a bulletin that went to all franchisees.

26. Any statements made by Midas when the 1981 Franchise Agreement was introduced concerning a 14.5% discount on prices are irrelevant to the Plaintiff 405341 for the following reasons:

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- (a) Midas' decision to offer a 14.5% discount was made approximately 8 years before 405341 entered into its Franchise Agreement with Midas;
- (b) No representation about a 14.5% discount was ever made by Midas to 405341;
- (c) No representation about a 14.5% discount was ever relied upon by 405341;
- (d) 405341 did not suffer any damages as a consequence of any representations by Midas about a 14.5% discount;
- (e) 405341 entered into a release in 1992 in which 405341 released all claims between Midas and 405341, including all claims relating to the 1981 Franchise Agreement;
- (f) 405341's Franchise Agreement permits Midas to set the prices at which it sells products to 405341;
- (g) 405341's Franchise Agreement permits Midas to change prices at any time;
- (h) 405341's Franchise Agreement requires 405341 to pay a 10% royalty to Midas;  
and
- (i) 405341's Franchise Agreement contains an entire agreement clause.



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27. Any statements made by Midas at the time the 1981 Franchise Agreement was introduced concerning a 14.5% discount on prices are irrelevant to the Plaintiff Landsbridge because:

- (a) Midas' decision to offer a 14.5% discount was made approximately 24 years before Landsbridge entered into its Franchise Agreement with Midas;
- (b) No representation about a 14.5% discount was ever made to Landsbridge;
- (c) By the time Landsbridge purchased its franchise, Midas had ceased distribution of products and Landsbridge was therefore never offered, and never received, a 14.5% discount on any Midas product;
- (d) No representation about a 14.5% discount was ever relied upon by Landsbridge;
- (e) Landsbridge did not suffer any damages as a consequence of any representations by Midas about a 14.5% discount;
- (f) Landsbridge's Franchise Agreement permits Midas to set the prices at which it sells products to Landsbridge;
- (g) Landsbridge's Franchise Agreement permits Midas to change those prices at any time;

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- (h) Landsbridge's Franchise Agreement requires Landsbridge to pay a 10% royalty to Midas; and
- (i) Landsbridge's Franchise Agreement contains an entire agreement clause.

#### **Closure of the Midas Distribution System**

28. Historically, Midas' business included the manufacture and distribution of auto products.

29. By 2002, Midas' manufacturing and distribution business was suffering financially. Its sales of mufflers and exhaust systems had been in a steady decline for approximately three (3) years, in part because new cars were being manufactured with mufflers and exhaust systems that were made of stainless steel that lasted much longer than the previous non-stainless steel mufflers and exhaust systems. In addition, franchisees were choosing to buy automotive parts from sources other than Midas.

30. Midas needed to renew its credit facility but it was only able to obtain financing if it agreed to wind down its manufacturing and distribution division and use the proceeds to pay down its debt.

31. The Franchise Agreement expressly provided Midas with the right to stop selling products to franchisees if, in Midas' opinion, the continued sale of such products became

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“unfeasible, unprofitable or otherwise undesirable”. Section 3.2(a) of the Franchise Agreement provides as follows:

3.2(a) Midas agrees to sell to Franchisee, during the term of this Agreement and subject to the terms hereafter set forth, such quantities of those genuine Midas products referred to in Schedule A attached hereto as Franchisee may order from time to time, provided however, that Midas may at any time and from time to time, in its sole discretion discontinue the sale to all its franchisees of any product or products, if, in the opinion of Midas, the continued sale of such product or products becomes unfeasible, unprofitable, or otherwise undesirable, and upon such discontinuation, the license herein granted with respect to such product or products shall terminate unless Midas has provided for alternative sources of supply meeting its standards and specifications and expressly elects to continue such license subject to such standards and specifications. [emphasis added]

32. Midas acted lawfully, reasonably, and in good faith when it exercised its discretion to discontinue the sale of products. The sale of products had become unprofitable and undesirable. The agreement to exit manufacturing and distribution allowed Midas to restructure its debt and avoid bankruptcy.

33. Midas' exit from the manufacturing and distribution end of its business took place over time. It ceased distributing everything except exhaust systems at the end of 2003 and ceased manufacturing exhaust systems in or about December 2005. Midas closed its final exhaust distribution centre, located in Chicago, Illinois, in March of 2006.

34. Every franchisee (including Landsbridge) that entered into a new Franchise Agreement or took an assignment of a Franchise Agreement in or after 2004 (i.e. after the

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implementation of the new supply chain program with Uni-Select) never experienced, and therefore could not have expected or relied on there being, a Midas owned distribution system during the term of its Franchise Agreement. Accordingly, such franchisees neither received, nor could they reasonably expect to receive, any discounts on products.

35. Contrary to the plaintiffs' allegation in paragraphs 31 and 39 of the statement of claim, nothing in s. 3.2(a), or any other section of the Franchise Agreement, obligates Midas to provide franchisees with a substitute distribution system.

36. Midas specifically denies the allegation in paragraph 29(d) of the statement of claim that it breached its obligation in sections 5.2 and 5.3 of the Franchise Agreement regarding warranties and guarantees. Under s. 5.2 of the Franchise Agreement, products purchased by franchisees from Midas are covered by a 90-day warranty. Under s. 5.3 of the Franchise Agreement, Midas offers a guarantee on certain products purchased by franchisees, but Midas is contractually permitted to discontinue the guarantee at any time. Midas always complied with sections 5.2 and 5.3 of the Franchise Agreement and honoured all of its warranties and guarantees. Contrary to the allegation of the plaintiffs, these sections do not prohibit Midas from ceasing distribution of products (which would be in conflict with the Midas' express right in section 3.2(a) to cease distributing products).

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### **Funding the Midas Warranty**

37. One of the hallmarks of the Midas brand is the lifetime warranty provided on genuine Midas products.

38. The Franchise Agreement provides that franchisees are required to honour warranty claims made by customers regardless of whether that franchisee sold the product to the customer. Midas reimburses franchisees for warranty-related expenses.

39. When Midas manufactured and distributed products, Midas funded its warranty obligation through the revenue generated by product sales to franchisees. The price paid by franchisees for products included an amount that covered warranty expenses.

40. After Midas ceased manufacturing and distributing products, it remained committed to continuing the lifetime warranty program (although it was not obligated to do so), and was prepared to accept all past and future warranty obligations to franchisees and consumers even though it was no longer selling automotive products that were the historical source of funding for the warranty program.

41. Midas' voluntary commitment to fund the warranty was, however, predicated on Uni-Select's agreement to make payments to Midas to fund warranty obligations and Midas' ability to add other suppliers to the supply chain program who would also pay rebates to Midas to fund the warranty program. Midas therefore funded its warranty obligation through payments

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received from Uni-Select. For franchisees, the price paid for products from Uni-Select therefore still included an amount to cover warranty expenses.

42. Contrary to the allegation in paragraph 44 of the statement of claim, the payments from Uni-Select to Midas did not have an inflationary effect on the prices charged to the plaintiffs for products. In fact, Uni-Select was required under the supply agreement to freeze the prices of most products at the price that Midas had been charging unless Uni-Select's direct product costs increased. For the products that experienced a price change, the net effect for most (if not all) franchisees was a net decrease in the price paid for products.

43. In December 2005, the Supply Agreement with Uni-Select was amended to include the supply of Walker exhaust products. The amendment was necessary as a result of Midas' decision to cease manufacturing exhaust products.

44. Every franchisee (including Landsbridge) that received a disclosure document was made fully aware of all of the fees payable to Midas and of the rebate payable to Midas from suppliers that would be used to fund the warranty. The disclosure document delivered to Landsbridge provides in part, as follows:

#### **Rebates/Commissions/Payments**

The Franchisor and the Franchisor's associate, Midas International, have supply arrangements with certain vendors under which they may receive annually a volume bonus or rebate based on annual net purchases of products by franchisees. These bonuses and rebates, if they occur, are retained by the Franchisor or its associate but may be passed on to the

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franchisees, as described below. Midas International also enjoys typical discounts for prompt payment of invoices, for goods purchased by it from certain of its suppliers. These discounts are retained by Midas International.

As noted above, in July 2003, Franchisor entered into a supply agreement with Uni-Select, whereby franchisor appointed Uni-Select Inc. to serve as the exclusive supplier of Midas-brand products, as well as a non-exclusive supplier of non-Midas brand automotive replacement products to franchisees located in Canada. During the first twenty-four (24) months of the term of this supply agreement, the Franchisor will receive from Uni-Select Inc. an aggregate of \$5.2 million in order to help cover the ongoing costs to the franchisor of honoring Midas warranties. During the remaining term thereof, the franchisor will receive from Uni-Select, Inc. a nine percent (9%) rebate on net product purchases (as described in the supply agreement) purchased by Midas shops from Uni-Select Inc., to help cover the ongoing costs to the franchisor of honouring Midas warranties. [...]

45. Midas used the rebates received from Uni-Select exclusively to fund the Midas warranty program and for no other purpose.

46. The Franchise Agreement does not restrict the manner in which Midas funds the warranty, nor does it prohibit supplier rebates.

47. Neither the plaintiffs nor the putative class suffered any damages or deprivation as a result of the change in the way Midas funded its warranty.

#### **The IMDA and the Charter**

48. On or about October 11, 2004, the International Midas Dealers Association (the "IMDA") and Midas International formed the North American Supply Chain Council (the

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"Council") whose purpose was set out in the North American Supply Chain Council Charter (the "Charter").

49. The Charter was signed by the IMDA and by Midas International to document the objectives of the Council and to recognize the IMDA's and Midas International's commitment to pursuing the Council's objectives.

50. One of the objectives of the Charter was to provide the IMDA (whose members consisted of hundreds of Midas franchisees) with a forum for input into supply chain decisions. Another objective was to enable Midas and its franchisees to approach suppliers as a united front for the purpose of adding them to the supply chain program, securing lower prices from suppliers, and getting suppliers to pay into the Midas warranty fund.

51. Securing funding for warranties was a critical objective for Midas and the IMDA because many franchisees were concerned about Midas' willingness to continue its lifetime warranty program over the long term. These franchisees also wanted other vendors who were willing to pay Midas a warranty rebate to be added to the supply chain program in order to ensure Midas would receive adequate funding of the warranty program in the future and to diversify the choice of competitively priced products available to franchisees.

52. The Charter provides for Midas to receive a rebate from suppliers for warranties and thus recognizes that if Midas is to continue the lifetime warranty program, it needs a long-term source of funding for the program.



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### **Plaintiffs Have no Rights under the Charter**

53. Midas Canada is not a party to the Charter and therefore cannot have any obligations under the Charter.

54. Midas International has fulfilled all of its obligations under the Charter. However, even if Midas International did not fulfill its obligations under the Charter, the plaintiffs do not have any right to assert a claim on the basis of the Charter for two reasons: (i) the Charter is not a contract and cannot form the basis of a claim; and (ii) the plaintiffs are not parties to the Charter.

55. In the alternative, if the plaintiffs have rights under the Charter, the Charter provides that all supply agreements must require the supplier to provide a 5% rebate to all Midas shops "unless a lesser percentage is agreed to by the Council" and the Council approved all of the supply agreements. Therefore, the Charter was not contravened by Midas.

### **Fiduciary Duty**

56. Contrary to the allegations at paragraphs 40-53 of the statement of claim, Midas did not owe the plaintiffs a fiduciary duty to negotiate the supply agreement with Uni-Select on their behalf as an agent or otherwise.

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### **Unjust Enrichment**

57. Midas denies that it has been unjustly enriched. Midas denies that the plaintiffs have suffered any deprivation, much less a corresponding deprivation. All of the actions taken by Midas that are the subject of the Claim were permitted by the Franchise Agreement or the Charter, and Midas always exercised its discretion in good faith.

### **Derogation from the Grant**

58. Midas has never derogated from the grant of the license in section 1.1(c). That section provides as follows:

**Section 1.1 Grant of License:** Midas hereby grants to Franchisee, and Franchisee hereby accepts from Midas, the right, franchise and license, for the term and upon the terms and conditions hereafter set forth: [...]

(c) To purchase from Midas and to resell from the Shop those genuine Midas products listed in Schedule A attached hereto, and to sell and install said genuine Midas products in or from the Shop; [...]  
[emphasis added]

59. The licence set forth in section 1.1(c) is subject to the terms and conditions set forth in the Franchise Agreement. In particular, the license is subject to section 3.2(a) which expressly provides Midas with the right to stop selling products to franchisees if, in Midas' opinion, the continued sale of such products became "unfeasible, unprofitable or otherwise undesirable".

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60. As set out in paragraph 32 above, Midas acted lawfully, reasonably and in good faith when it exercised its discretion to discontinue the sale of products. The sale of products had become unprofitable and undesirable. The agreement to exit manufacturing and distribution allowed Midas to restructure its debt and avoid bankruptcy.

### **Damages**

61. Midas denies that the plaintiffs have suffered any loss or damage by reason of the matters set forth in the Claim. Alternatively, the loss or damage claimed by the plaintiffs is exaggerated, too remote to be recoverable at law, and the plaintiffs have failed to mitigate any such loss or damage.

62. Contrary to the allegation in paragraphs 80-81 of the Claim, the plaintiffs are not entitled to an audit of all warranty related revenues and expenses. There is no basis in common law, in equity, or under the Charter (to which the plaintiffs are not parties) for this remedy.

63. There is no basis upon which to award punitive, exemplary or aggravated damages in this action.

64. The defendants therefore ask that this action be dismissed, with costs on a substantial indemnity basis.

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Date: October 17, 2008

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<p></p>	<p><b>STATEMENT OF DEFENCE</b></p>
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