

**ONTARIO
SUPERIOR COURT OF JUSTICE**

BETWEEN:

2038724 ONTARIO LTD. and 2036250 ONTARIO INC.

Plaintiffs

- and -

**QUIZNO'S CANADA RESTAURANT CORPORATION, QUIZ-CAN LLC, THE
QUIZNO'S MASTER LLC, GORDON FOOD SERVICE, INC. and GFS CANADA
COMPANY INC.**

Defendants

Proceedings under the *Class Proceedings Act, 1992*

**STATEMENT OF DEFENCE OF THE DEFENDANTS
GORDON FOOD SERVICE, INC. AND GFS CANADA COMPANY INC.**

1. The defendants Gordon Food Service, Inc. ("GFS Inc.") and GFS Canada Company ("GFS Co.") (collectively, "GFS" or the "GFS Defendants") admit the allegations contained in paragraphs 9, 10, and 26 (except the second sentence) of the Amended Amended Amended Statement of Claim (the "Claim").

2. The GFS Defendants state that no factual allegations are made against them in paragraphs 2-4, 6-8A, 13-20, 23-24, 30, 40, 50-54, 65, and 73 of the Claim, and therefore no response to these paragraphs is required. To the extent a response is required, the GFS Defendants state that they have no knowledge sufficient to admit or deny these allegations.

3. The GFS Defendants state that no factual allegations are made against them in paragraphs 21-22, 31, 35-36, 46-47, 55, 55B, 55D, 55E, 55F, 55G, 67-68, 71, and 74 of the

Claim, and therefore no response to these paragraphs is required. To the extent a response is required, the GFS Defendants deny these allegations.

4. The GFS Defendants state that the allegations contained in paragraphs 28-29, and 56-61 are not directed to them and in any event are legal conclusions, and therefore no response is required. To the extent a response is required, the GFS Defendants deny these allegations.

5. The GFS Defendants state that the allegations contained in paragraphs 34, 38, 42, and 76 of the Claim are legal conclusions to which no response is required. To the extent a response is required, the GFS Defendants deny these allegations.

6. The GFS Defendants deny the allegations in paragraphs 5 (but admit that by Order of Perell J. dated November 23, 2009 (the "Certification Order"), the Plaintiffs have been appointed as representative plaintiffs of a class defined in paragraph 2 of the Certification Order), 11 (but admit that GFS Co. is incorporated under the laws of New Brunswick), 12, 25 (but admit that GFS Co. has a distribution agreement with Canada Food Distribution Company ("CFD") for the distribution of food and other supplies to Canadian Quiznos franchise stores and that the identified affiliates of GFS Co. (as corrected below) distribute same to such stores (as further described below)), 26 (second sentence only, but admit that GFS Inc. is headquartered in Grand Rapids, Michigan), 27 (but admit that affiliates of GFS Co. distribute food and other supplies to Canadian Quiznos franchise stores, most of which purchase a majority of same directly from a GFS Co. affiliate), 32-33, 37, 39, 41, 43-45, 48-49, 55A, 55C, 62-64, 66, 69-70, and 71A (but admit that GFS and CFD entered into a distribution agreement in or about October 2006).

7. The GFS Defendants deny that they or GFS employees have acted unlawfully as alleged or otherwise, and deny that the Plaintiffs are entitled to the relief requested as against the GFS Defendants in paragraphs 1, 66A, 72, 75, and 75A of the

Claim, or to any relief as against GFS. The GFS Defendants specifically deny that the Plaintiffs have suffered any damages from the conduct of GFS, and put the Plaintiffs to the strict proof thereof.

Overview

8. The GFS Defendants state that they have been improperly dragged into this litigation, which is a franchise dispute between the Plaintiffs and their Quiznos franchisors (the "Quiznos Defendants"). The overwhelming majority of the Plaintiffs' allegations (and claims) in their pleading are not made against GFS at all. The Plaintiffs plead at length and apparently rely upon various provisions in franchise agreements with the Quiznos Defendants to which GFS is not a party and with which it had and has no involvement. The GFS Defendants clearly are not the cause of the Plaintiffs' complaints about the Quiznos franchise system. Fundamentally, all GFS does and wants to do is provide distribution services to the Quiznos franchisees, as contractually agreed with Quiznos.

9. GFS has not unlawfully "conspired" with any Quiznos entity. By distribution agreement, GFS Co. has been appointed the primary distributor of food and other products to Quiznos' Canadian franchise stores, and in that capacity its affiliates (collectively, the "GFS Companies") perform limited distribution, warehousing, and logistics functions for the Quiznos system.

10. The GFS Companies purchase the substantial majority of all products sold and distributed to Quiznos stores, many of which are made according to specifications created by Quiznos, from a Quiznos entity directly or from vendors designated by Quiznos at prices negotiated between the Quiznos entity and those vendors, and as such GFS does not control the prices charged to GFS for those products. In exchange for the sales and distribution services they perform, the GFS Companies charge Quiznos stores a commercially reasonable mark-up on their product cost, in

accordance with the terms of the distribution agreement. By agreeing to sell and distribute products to Canadian Quiznos franchises pursuant to its distribution agreement, GFS has not unlawfully conspired or “aided and abetted” price maintenance by the Quiznos Defendants.

11. GFS states that there is no basis for the allegations made against them by the Plaintiffs and that the Claim should be dismissed as against the GFS Defendants with costs on a substantial indemnity scale.

GFS’ Canadian Business Operations

12. Although named as a defendant in this action, GFS Inc. is a company incorporated under the laws of Michigan, United States of America, which does not provide any product sales or distribution services in Canada.

13. GFS Co. is a company incorporated under the laws of New Brunswick that is also registered to do business in the province of British Columbia. Contrary to the allegations in paragraphs 11 and 12 of the Claim, GFS Co. does not carry on business throughout Canada or in Ontario.

14. The five GFS Companies (four of which are identified in paragraph 25 of the Claim), which are affiliates of GFS Co. and indirectly are subsidiaries of GFS Inc., provide sales and distribution services in various parts of Canada, including to Quiznos franchise stores, as follows.

15. GFS British Columbia Inc., formerly known as Neptune Foodservice Inc. (“GFS BC”) is a federally incorporated company with its registered office in Calgary, Alberta which provides services in British Columbia. GFS BC has a distribution centre located in Delta, British Columbia.

16. GFS Prairies Inc., formerly known as Bridge Brand Food Services Ltd. (“GFS Prairies”), is an Alberta corporation with its registered office in Calgary, which

serves Alberta, the Northwest Territories, Saskatchewan, Manitoba and northwestern Ontario. GFS Prairies has distribution centres in Calgary, Edmonton and Winnipeg.

17. GFS Ontario Inc. ("GFS Ontario") is an Ontario corporation with its registered office in Toronto, which provides services to all parts of Ontario other than the northwest. GFS Ontario has a distribution centre in Milton, Ontario.

18. GFS Quebec Inc., formerly known as Distal Inc. ("GFS Quebec"), is a Canadian corporation which provides distribution services in the province of Quebec. GFS Quebec has distribution centres in Boucherville (near Montreal) and Beauport (near Quebec City).

19. GFS Atlantic Inc., formerly known as M&S Food Service Inc. ("GFS Atlantic"), is a company incorporated under the laws of New Brunswick with its registered office in Amherst, Nova Scotia, which serves New Brunswick, Nova Scotia and Prince Edward Island. GFS Atlantic has a distribution centre located in Amherst, Nova Scotia.

20. In broad terms, the GFS Companies' core business operations are: purchasing desired products from manufacturers or suppliers, warehousing and maintaining proper inventory levels of the products, and selling and delivering the products to their customers as and when needed. The GFS Companies' customers include a variety of locally, regionally, or nationally-based businesses, including single restaurant operators, regional restaurant chains, and quick-service restaurant franchise operations with stores across Canada.

21. Each of the GFS Companies is a "broad line" distributor which purchases, stocks, sells, and delivers a wide array of food and beverages, as well as related food service products (such as cups, lids, containers, straws, dispensers and cleaning supplies). The GFS Companies offer various food products for sale under the "GFS" brand name, and other brand names owned by GFS. The GFS Companies also offer a

wide range of well-known manufacturers' brand name products for sale and distribution.

22. Although certain products are available from each of the GFS Companies, each company (and distribution centre) has different products available for sale. The GFS Companies acquire products from a wide variety of vendors, including large national or North American manufacturers, regional suppliers, and smaller locally based operations. The GFS Companies' larger distribution centres, such as the Delta, Calgary or Milton locations, will have approximately 15,000 different items on offer at any given time.

23. GFS has tried to organize its Canadian food distribution business to maximize cost efficiency and customer satisfaction in the food distribution business, by balancing the potential economies of scale created by larger volume purchases, bigger warehouses and broader customer bases, against the need to be able to satisfy the very common demands of restaurant operators for prompt order filling of quick "next day" deliveries, which requires a certain proximity to the customer.

24. Depending on the needs and preferences of the particular customer, each GFS company may provide services other than stocking, selling and delivering products described above. The GFS Companies work closely with the certain customers to create menus, develop product specifications, and identify sources for desired "custom" product offerings. Not all customers use these services, however, and none of the GFS Companies performs any such services as distributors to Canadian Quiznos franchise stores. Those services are performed for the Quiznos franchise system by Quiznos.

GFS' Distribution Services to Canadian Quiznos Franchises

25. As stated above, GFS Co. has been appointed the primary distributor of products to Quiznos franchise stores in Canada pursuant to a distribution agreement with CFD.

26. Pursuant to that distribution agreement, each of the five GFS Companies sells and distributes products to Quiznos franchises, depending on the location of the store (for example, GFS BC sells and distributes products to Quiznos stores located in British Columbia). There are also Quiznos franchise stores located in Newfoundland that are not directly served by a GFS company, but rather by an independent distributor with which GFS has a distribution arrangement.

27. As stated above, the GFS Companies' role as distributor to the Quiznos stores is limited. The GFS Companies acquire and maintain an appropriate inventory of products, deliver products ordered by Quiznos stores, and invoice the stores for payment. In return, each GFS Company is entitled to and does charge a commercially reasonable mark-up on products sold, in accordance with the distribution agreement.

28. CFD, not GFS, determines which products are approved for distribution. CFD alone determines the specifications for the products it approves. For the substantial majority of items (the vast majority by product sales volume), CFD negotiates the price at which GFS acquires the product from the supplier/manufacturer. And CFD alone determines whether it will charge GFS a "sourcing fee" on the product, and, if so, the amount of that fee.

Products

29. The GFS Companies offer hundreds of products for sale and distribution to Quiznos franchise stores. These products include a wide range of food items (such as bread, cheese, meat, vegetables, soup, potato chips, cookies, cakes, sauces,

condiments, salad dressings, soft drinks and milk), and various food service products (including cleaning products, garbage bags, brooms, cups, lids, and straws). Not all products which are available to Quiznos stores served by one GFS Company are available to those served by other GFS Companies, however.

30. Although GFS Co. has been appointed the primary distributor to Canadian Quiznos franchises, the Quiznos stores are not required to purchase all products used in their stores from a GFS Company. Although the GFS Companies offer various produce items for sale, Quiznos franchise stores are not required to purchase any of these products from them – and many stores do not.

31. Even with respect to products that Quiznos franchise stores are supposed to obtain from the GFS Companies, they do not always do so. Quiznos stores have obtained products from other unauthorized sources. The incidence and extent of such unauthorized “grey market” purchases by Quiznos stores has varied over time.

32. The products that the GFS Companies obtain for sale and distribution to Quiznos franchise stores originate from dozens of different manufacturers/vendors. Some similar items for sale to Quiznos stores may be obtained by one GFS Company from one supplier, and obtained by another GFS Company from a different supplier.

33. For the substantial majority of products (representing an even greater percentage of total sales volume), the GFS Companies do not negotiate prices with the supplier. In the case of “company buy/sell products”, as defined in the distribution agreement, CFD negotiates a price and purchases each product from the manufacturer/vendor, and then resells it to the GFS Companies. In the case of “company contract products”, as defined in the distribution agreement, CFD negotiates the contract price at which the GFS Company acquires the product directly from the manufacturer/vendor.

34. It is only with respect to a few food items (such as certain cheeses) and some largely generic supplies (such as toothpicks and stir sticks) that the GFS Companies negotiate prices directly with the manufacturer/vendor of the product.

35. The distribution agreement between CFD and GFS Co. provides the method for calculating product prices that the GFS Companies are contractually entitled to charge Quiznos franchise stores.

36. The primary elements of each product's price to the Quiznos stores are: the cost of the product (for most products, a cost either determined by CFD or negotiated by CFD) to the GFS Company; the sourcing fee charged by CFD, if any; and the mark-up that the GFS Company charges for the sale and distribution services it provides. These factors cause pricing by the GFS Companies to Quiznos franchise stores to vary product by product, region by region, distribution centre by distribution centre.

Orders and Deliveries

37. Each month, each GFS Company sends an ordering guide to the Quiznos stores it serves which lists the products available for purchase and the price for each product in effect at the beginning of each month. For much of the class period, the ordering guides cannot be relied upon to determine the actual price paid by Quiznos stores for products throughout any particular month, however, as the prices for some products changed on a weekly basis, based on market conditions and/or U.S. currency exchange rates.

38. In addition, actual prices paid by Quiznos stores for products at any time can be (and have been) affected by differences in credit/payment terms, eligibility for rebate programs offered by Quiznos, and unauthorized "grey market" purchases, which have varied across Quiznos franchise stores and over time.

39. Most Quiznos stores place orders with the GFS Company serving them on a weekly basis and receive deliveries once per week. The weekly volume of products ordered varies significantly across Quiznos franchises in Canada, ranging from low volume stores ordering 40 cases per week to high volume stores ordering 300 cases per week. (The term "case" refers to one packaged unit of the particular product to be shipped.) Quiznos stores ordering more than 150 cases are entitled to receive two deliveries per week.

GFS' "With Prejudice" Offer to the Plaintiffs

40. After this litigation was commenced, GFS made a "with prejudice" proposal in an effort to be removed from the litigation. The proposal was directed to Quiznos Denver Subs Canada ("QDSC"), the group which the Plaintiffs have identified as representing the Quiznos franchisees, and through which a group of franchisees could purchase in significant volumes (recognizing that not all franchisees are members of QDSC, therefore volumes through that organization would not be as great as those made through the present Quiznos franchise system).

41. The purpose of making the proposal was to communicate that the GFS Companies are prepared to provide distribution services to a large group of franchisees in respect of all products for which approval has been granted by the Quiznos franchisor or for which such approval is not required.

42. The proposal made to the franchisees (through QDSC) identified key features of the proposed arrangement, but contemplated further negotiation of important details.

43. The core of the proposal was that GFS would provide distribution services to the QDSC franchisees on a cost-plus basis, with a mark-up scale that varied according to the national average of cases ordered by the franchisees per delivery. The mark-up scale in the current distribution agreement between GFS Co. and CFD

also varies according to same range of cases per delivery as set out in the proposal to QDSC, but the mark-up associated with each case range in the proposal is higher. This reflects the fact the proposal rates were calculated using the assumption that only 250 stores would participate, rather than the more than 400 stores covered by the current distribution agreement.

44. The GFS proposal also provides that with respect to each product that would be distributed by the GFS Companies, the parties would give consideration to whether the Plaintiffs could purchase that product through the GFS Companies, either as one of the GFS brand products, or one of the manufacturer-branded products that each of the GFS Companies regularly stocks. As stated above, the substantial majority of products currently distributed to Quiznos stores do not fall into either category.

45. GFS also proposed several basic terms that would help reduce costs and maximize distribution efficiencies: a credit to franchisees for electronic orders, a requirement that payment be made by direct electronic funds transfer, the potential for deliveries to be made on any day of the week, and for after-hours deliveries (using a key and drop-box). In the restaurant business, certain days of the week (e.g. Monday and Friday) are very popular for deliveries. The possibility of making deliveries to Quiznos franchisees on other days of the week would permit the GFS Companies to use their truck and driver fleet more efficiently, by evening out the daily workload.

46. As stated above, one of the premises of the proposal to QDSC was that the franchisees had secured approval from the Quiznos franchisor(s) for the product(s) to be distributed, or that no such approval was required. The GFS Companies made clear that, as distributors, they have no role to play in this product approval process.

47. The franchisees, either through QDSC or otherwise, have not pursued the GFS proposal.

GFS Has Not Engaged In A "Civil Conspiracy"

48. At paragraph 32 of the Claim, the Plaintiffs allege in support of their sole "civil conspiracy" claim against the GFS Defendants that the "Quiznos defendants have entered into oral and/or written agreements (the Price Maintenance Agreements'), directly or indirectly, with each of the GFS companies and other manufacturers and/or suppliers", purportedly to "enhance, fix and maintain the prices" for products sold by the GFS Companies to Quiznos franchise stores. GFS denies that it has entered into any Price Maintenance Agreement with any Quiznos entity.

49. Although the Claim purports to "set out more fully" the "nature" of the alleged Price Maintenance Agreements at paragraphs 55A to 55G, in those paragraphs the Plaintiffs simply make vague reference to a "CFD-GFS arrangement" which purportedly was "for the purpose of inflating the prices" paid for products by Canadian Quiznos franchise stores. The GFS Defendants deny that GFS has acted with any unlawful or improper purpose with respect to the distribution of products to Quiznos stores in Canada and state that the "arrangement" between GFS and CFD is as set out in the parties' distribution agreement and is perfectly lawful. The GFS Defendants deny that the distribution agreement constitutes an unlawful "conspiracy" with Quiznos for the commission by Quiznos of price maintenance or otherwise.

No Basis For The Allegations of Criminal Conduct Against GFS Employees

50. At paragraph 63A of the Claim, the Plaintiffs allege that certain named GFS employees and "others including senior managers" engaged in communications said

to constitute "aiding, abetting and counselling" the commission of illegal price maintenance, "contrary to sections 21 and 22 of the Criminal Code, R.S.C. 1985, c.C-46." The GFS Defendants deny these allegations and state that the ascription of criminal conduct and motives to GFS employees by the Plaintiffs in their Claim is wholly without foundation. GFS states that the communications by its employees with employees of Quiznos have been (and are) made in the ordinary course of lawful business activities, being the provision of distribution services to the Canadian Quiznos franchise system.

51. GFS requests that this action be dismissed, with costs on a substantial indemnity basis.

December 7, 2009

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ONTARIO INC.

Plaintiffs

QUIZNO'S CANADA RESTAURANT
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Court File No: 06-CV-311330CP

ONTARIO
SUPERIOR COURT OF JUSTICE

Proceeding commenced at Toronto

**STATEMENT OF DEFENCE OF THE
DEFENDANTS
GORDON FOOD SERVICE, INC. AND GFS
CANADA COMPANY INC.**

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