DISTRICT COURT, CITY AND COUNTY OF DENVER, STATE OF COLORADO 1437 Bannock Street Denver, Colorado 80202	
QUIZNOS FRANCHISING II, LLC, Plaintiff, v. ZIG ZAG RESTAURANT GROUP, LLC, et al., Defendants.	Case No. 06CV10765 COURTROOM 3
ORDER	

This case is before me following a five-day bench trial that began December 8, 2008. Based on the evidence and arguments presented at that trial, I find and conclude as follows.

I. FINDINGS OF FACT

A. Introduction

Most of the facts were undisputed. Plaintiff Quiznos Franchising II, LLC ("Quiznos") is a franchisor of toasted sub sandwich fast-food restaurants. Defendant Zig Zag Restaurant Group, LLC ("Zig Zag") is a Pennsylvania limited liability company formed by the individual Defendants, Richard Piotrowski and Ellen Blickman. Piotrowski and Blickman, who are husband and wife, are the only members of Zig Zag, which they formed for the purpose of owning and operating a Quiznos franchise. Unless otherwise specified, when I refer to "Defendants" I mean the individual Defendants Piotrowski and Blickman.

As discussed in more detail below, Defendants entered into two franchise agreements with Quiznos, but ended up operating only a single store, in Coopersburg, Pennsylvania. They operated the Coopersburg store for only eight months, at the end of which their franchise agreement was purportedly terminated by Quiznos because Quiznos allegedly determined Defendants had intentionally under-portioned the meat on a single sandwich.

Quiznos brought this action claiming, among other things, that Defendants breached both franchise agreements, and Defendants counterclaimed for breach of the Coopersburg agreement and rescission of the unused agreement.

B. The Oxford Location

Defendants were working and living in northern New Jersey when they decided, in late 2003, to relocate outside of the New York City metropolitan area and open their own business together. They testified that it was their dream to get out of the city and work together in some kind of family business. So they moved to Bethlehem, Pennsylvania (about 70 miles north of Philadelphia) and later to Allentown (10 minutes from Bethlehem) and began to research franchise opportunities.

Defendants attended a Quiznos franchising seminar in November 2004, and in December 2004 they decided to buy a Quiznos franchise. On December 29, 2004, they entered into a "Quiznos Franchising LLC Franchise Agreement" (Exhibit 26), which I will refer to as the "8859 Agreement,"[1] and paid Quiznos the required $25,000 franchise fee. At the time they entered into the 8859 Agreement, Defendants had not yet identified a location for the store. (Under the Franchise Agreements, Quiznos franchisees are responsible for finding and leasing their own store

[1] Quiznos Franchise Agreements are identified by a unique franchisee or store number, and 8859 was the number assigned to this initial Agreement.

space, with Quiznos' approval.) Defendants worked for several months, with the assistance of Quiznos real estate personnel, trying to find a suitable location near their home, and eventually settled on a space inside a yet-to-be-built mall in Oxford, Pennsylvania, a town about 50 miles west of Philadelphia and 100 miles southwest of Bethlehem/Allentown. Defendants even signed a lease with the mall developer. But the mall was never built, and ultimately the developer and Defendants executed a mutual release of their obligations under the lease.

Defendants have never operated a franchise under the 8859 Agreement, contrary to ¶ 6.9 of that Agreement, which requires the franchisee to begin operating a Quiznos store within 12 months of the execution of the Agreement. On April 17, 2006, almost 16 months after signing the 8859 Agreement and therefore after the 12-month deadline had already expired, Defendants specifically raised the issue of the 12-month deadline with Quiznos officials. Michael Daigle, Quiznos' general counsel, responded with an e-mail to Defendants' then-lawyer, stating "Ms. Blickman and Mr. Piotrowski are not at risk of having their franchise agreement terminated and, to my knowledge, we have not threatened that. . . . If it would make them feel more comfortable, I would be happy to send them our standard form of amendment to the franchise agreement to extend the term." Exhibit 27. There is no evidence that Defendants, their then-lawyer or Quiznos followed up to re-set any deadline, and this issue was ignored by both parties until after this lawsuit was filed.

C. The Coopersburg Location

While Defendants were still working on the Oxford location, Quiznos' real estate personnel advised them of an opportunity to work at, if not acquire, an existing Quiznos franchise in Coopersburg, Pennsylvania, a town just 10 minutes south of Bethlehem/Allentown. The owner of that franchise, a Mr. Alan Sterner, was looking for a full-time manager. Defendants decided it would be a great learning experience to operate a Quiznos franchise while their Oxford location was being built. So Mr. Piotrowski agreed to become Mr. Sterner's full-time manager, and he ran the Coopersburg store from early July 2005 until Defendants bought it effective February 2006.

When Sterner decided to sell the store, Defendants expressed an interest in buying it even though the Oxford location was not yet dead, since their long-term plan was to own more than one Quiznos franchise anyway. Defendants and Sterner eventually agreed to the terms of a sale in September 2005 (see Asset Purchase Agreement, Exhibit 9), though it took time for Defendants to make the necessary financial arrangements, and the sale did not close until February 1, 2006. The transfer was accomplished by Zig Zag taking an assignment of Sterner's existing lease (Exhibit 8) and Defendants taking an assignment of Sterner's Franchise Agreement with Quiznos, which I will refer to as "the 6309 Agreement." Quiznos consented to the transfer, upon payment of a $12,500 transfer fee. The 6309 Agreement itself, its assignment and assumption from Sterner to Defendants and Quiznos' written consent to the transfer were all admitted as Exhibit 2. The lease and assignment were admitted as Exhibit 8.

The general terms of the sale were these: the price was $200,000, $70,000 down and the balance of $130,000 from an SBA loan taken out by Zig Zag and guaranteed by Defendants. Zig Zag borrowed an additional $20,000 on the SBA loan for working capital (for a total loan of $150,000). Sterner paid Quiznos the $12,500 transfer fee out of his proceeds. Exhibit 10.

Defendants operated the store as owners from February 1, 2006 through Quiznos' purported termination of the 6309 Agreement in early October 2006. Defendants worked 10- to12-hour days, six to seven days every week, along with some paid help. As discussed in much greater detail below, through their own hard work Defendants were largely able to stabilize what had been a rather steady decline in profitability during the end of Mr. Sterner's ownership.

D. Quiznos' Field Tests

The seeds of this case were planted in the summer of 2006, when Quiznos decided to begin an aggressive national advertising campaign targeting its main competitor, Subway. The centerpiece of the campaign would be a new sandwich, the Prime Rib Philly Cheesesteak, which would be touted as having "more than twice the meat" of a comparable Subway sandwich. Despite the fact that this claim was demonstrably true based simply on the specifications of each sandwich (5 oz. to be placed on the small Quiznos sandwich, 2 oz. on the small Subway, with equivalent proportions for larger versions), Mr. Daigle decided Quiznos had to take the extra step of satisfying itself that the new sandwiches were actually being built to specifications, and therefore did in fact have twice the meat of Subway's. Mr. Daigle testified that he made this decision for two reasons—to satisfy advertisers about the truth of the claim, and to protect Quiznos from any litigation by Subway (which litigation in fact occurred anyway).

Mr. Daigle commissioned Michael Manning, Quiznos' vice-president in charge of quality control, to design a test for anonymous Quiznos personnel—called "mystery shoppers"—to conduct at every one of Quiznos' 4,000-plus U.S. franchises. Mr. Manning designed the following test: Mystery shoppers would call the store and order a small Prime Rib Philly Cheesesteak to go. The mystery shopper would then pick up the sandwich, remove its contents from the bread, take off all the onions, attempt to separate the melted cheese from the meat (being instructed never to remove any meat), weigh the meat, and record and report the meat's weight.

As mentioned above, the small Prime Rib Philly Cheesesteak is supposed to be made with 5 oz. of pre-cooked prime rib, before being cooked further in au jus and then run under a toaster. Mr. Manning determined, as discussed in much greater detail below, that if the meat weighed less than 4.5 oz. after these processes, one could reliably infer that the sandwich started off with less than the required 5 oz.

If mystery shoppers discovered a sandwich with less than 4.5 oz., they were instructed to make three inquiries regarding whether the shortage was "intentional': 1) check the store scale to see if it had been altered; 2) check the job aids (the actual in-store specifications on how to build sandwiches) to see if they had been altered; and 3) ask the person who made the sandwich how much meat he/she put on it.

George Wooten, then the Quiznos vice-president for field operations, was in charge of training his field operators to be the mystery shoppers. He instructed all of them, in writing, that if a sandwich failed the test (that is, the meat weighed less than 4.5 oz.), they were to do a second test "the next day or by the end of next week." E-mail from G. Wooten to M. Daigle dated September 19, 2006, Exhibit 71. See also Exhibit 41. Despite the fact that this e-mail was sent to Mr. Daigle, these second field tests were never done, and franchisees like Defendants were defaulted or terminated based on a single test of a single sandwich weighed on a single day.

There was one additional and important piece of evidence about the "intentionality" inquiry by the mystery shoppers. At some unspecified time after all the field tests were completed and the results reported and recorded, someone at Quiznos did some sort of re-examination of the "intentionality" findings by the mystery shoppers. Many of the results originally reported as "intentional" under-portioning, including Defendants', were re-classified as something less than intentional. In Defendants' case, as with many others, the results were re-classified as "Not 100% intentional." Exhibit 64. None of the Quiznos witnesses could explain this re-classification, and it appears that Mr. Daigle and his legal department were entirely unaware of it. Whether aware or unaware, Mr. Daigle and the legal department never considered this re-assessment in their dealings with Defendants.

In terms of taking action in response to the test results, Mr. Daigle testified that he decided he would have his staff automatically send out facially non-curable notices of termination to every franchisee whose tests resulted in a weight of less than 4 oz., and curable notices of default to every franchisee who tested at or above 4 oz. but less than 4.5 oz., unless, in this latter range, the shortage was "intentional" as determined by the mystery shopper's three-step process described above, in which case even franchisees in the 4.0 to 4.5^{-} range would be terminated. By the way, there was only a single form notice of termination, which did not distinguish between franchisees "unintentionally" below 4 oz. and those "intentionally" at or above 4 oz and below 4.5 oz., so franchisees like Defendants, who were at 4.0 oz. but who were nevertheless terminated for intentional under-portioning, were not informed in the notice of any allegations of intentional under-portioning.

In actual application, however, Mr. Daigle and the legal department did not follow their own protocol. Exhibit 67 is a summary of the final weights of some of the tests, and the initial actions taken by Quiznos. That Exhibit shows that there were many franchisees (by my count at least 32) who tested below 4 oz. and nevertheless received a notice of default rather than a notice of termination. Several of these franchisees tested as low as 2.5 oz. Conversely, there were a handful of franchisees who tested at 4.5 oz. and who were nevertheless defaulted. Neither Mr. Daigle nor any other Quiznos witness could explain these results.

Not only did the legal department not enforce the protocol consistently, it misrepresented the details of the protocol to other Quiznos officials. When field personnel began to complain about the idea of terminating franchisees based on these tests, the legal department told Mr. Wooten that no franchisee would be terminated except for an "egregious shortage." Wooten then passed that information on to the field in writing, adding that in his view an "egregious shortage" would be something as low as 3.0 oz. Exhibit 49. But of course that was not at all an accurate description of the protocol Mr. Daigle designed and (albeit inconsistently) implemented.

Mr. Daigle also testified that Quiznos really had no interest in terminating any franchisees without giving them an opportunity to get back into compliance.[2] So Mr. Daigle developed the following procedure to deal with franchisees who failed the test: Even though the notices of termination were on their face unconditional and unequivocal, and demanded that the franchisee immediately stop operating, if franchisees contacted Mr. Daigle at the e-mail address or phone number contained in the last sentence of the notice of termination (in which they were invited to contact Quiznos with any questions), Mr. Daigle's staff would automatically send them a form e-mail advising them that in fact they did not need to stop operations, and that the notice of termination would be rescinded if they passed a future third-party inspection.[3]

In turns out that despite its inconsistent application of the Daigle protocol, Quiznos still sent notices of termination to approximately 300 franchisees, more than 7% of its total number of U.S. franchisees. One or two never responded and were therefore terminated. Defendants were the only responding franchisees who were not given a chance to have the termination rescinded if they passed a third-party inspection.

It is clear to me, and I find, that this whole charade of "terminating" and "defaulting" franchisees who failed the field test was just that—a charade—driven not by Quiznos' genuine concern about whether its franchisees were making sandwiches to spec, but rather by its overriding

[2] One might therefore ask, as I did at trial, what the real difference was between a curable notice of default and a purportedly non-curable notice of termination, if in both cases franchisees could continue to operate and could cure. No Quiznos witness could adequately explain the difference. The reality, as discussed below, is that both notices were just for show, so the difference between them didn't matter.

[3] This third-party inspection is not to be confused with Mr. Wooten's second round of field tests, which, as mentioned above, never took place.

public relations desire to be able to proceed with its national advertising campaign targeting Subway. But the public relations monster had to serve two masters—the action Quiznos took once it ferreted out non-complying franchisees had to *look* serious (otherwise what would Subway say?), but it couldn't actually *be* serious, unless Quiznos was willing to lose a potentially huge number of non-complying franchisees, which it was not.

This explains the sort of non-termination termination process Mr. Daigle came up with. What he did not count on was that franchisees like Defendants might actually take the notice of termination at face value.

E. The Purported Termination of Defendants' Franchise

A mystery shopper visited Defendants' store in late September 2006. Quiznos' records are not entirely clear, but I find that the mystery shopper was a Mr. Eric Sanata, and that he visited Defendants' store on September 20, 2006. Exhibit H; cf. Exhibit O. Quiznos' summations of Mr. Sanata's reported results show that Mr. Sanata measured Defendants' sandwich meat at 4.00 oz. Exhibit H. Ordinarily, then, according to Mr. Daigle's protocol, Defendants would have gotten only a default notice. But because the summary of Mr. Sanata's test results also indicated that he found Defendants had "intentionally" under-portioned the meat, id., Mr. Daigle's staff sent Defendants the form notice of termination. Exhibit 1.

Quiznos could not produce Mr. Sanata's test form or any other notes he may have taken contemporaneous with the test. Nor was either side able to locate Mr. Sanata. As a result, we have no details about the particular test he performed (except to assume he attempted to comply with Messrs. Manning's and Wooten's instructions). More importantly, we have no idea why Mr. Sanata concluded that Defendants had intentionally shorted the meat on the sandwich—whether he discovered an altered scale or job aids, or whether Defendants or an employee admitted under-portioning. Defendants, on the other hand, both testified that they never intentionally under-portioned any of their sandwiches, and never instructed any employee to do so. I believed that testimony. Moreover, as mentioned above, Quiznos in any event re-classified Defendants' under-portioning as "Not 100% intentional."

The notice of termination sent to Defendants, as was presumably true of all the notices of termination, erroneously stated that the mystery shopper had determined that Defendants were using only 4.00 oz. of meat "in preparing the sandwich." Exhibit 1. But of course this number was the tested post-preparation weight that Quiznos used to infer that the actual starting weight was less than the required 5 ounces.

As with all of the notices of termination, Quiznos' notice of termination of Defendants' franchise was sent by overnight carrier. The carrier attempted delivery at Defendants' home on the morning of Tuesday, October 3, 2006, but, ironically, there was no one home to accept the delivery because Defendants had already left to open their store. The carrier left a notice of attempted delivery, and Defendants actually received the notice in the morning of the next day, Wednesday, October 4, 2006, at around 9:00 a.m., shortly before they would otherwise drive to the store to open up. Aware that both the notice of termination itself and the terms of the 6309 Agreement required them to shut the store immediately upon a notice of termination, Defendants decided they should not open.

Mr. Piotrowski then made a seemingly innocuous, but fateful, decision. Rather than e-mailing Mr. Daigle at the address provided in the notice of termination—in which event he would have automatically received the form e-mail telling him not to close and that the termination would be rescinded if he passed a third-party inspection—Mr. Piotrowski instead called the telephone number that was also listed in the notice of termination as an alternative method of contact. Not surprisingly—because presumably dozens if not hundreds of franchisees were also calling that number—Mr. Piotrowski could not get through to a live person, and left a message. He, and on one occasion Ms. Blickman, continued to call Mr. Daigle and other Quiznos officials throughout the rest of the day (by my count, at least 20 times), never getting through to anyone, and never having anyone return any message.

Defendants' messages grew more and more frantic and frustrated. Those messages are in evidence in the form of transcripts, Exhibit I, and some of them were preserved audially in Exhibit W. I find that those messages were, on the whole, remarkably restrained, given that Defendants' livelihood had apparently just been snatched away by a letter claiming that an unidentified person had on one occasion detected an unidentified worker at Defendants' store under-portioning the meat on a single sandwich by a full ounce (remember, the notice erroneously claimed the test showed the sandwich started out at 4.00 oz.). Most of these messages, at least early on, simply stated that Defendants had closed their store in compliance with the notice of termination, denied any under-portioning, and requested a return call.

At 10:00 a.m., after an hour of leaving phone messages, Mr. Piotrowski e-mailed the Quiznos' "Help Desk," a Quiznos information service provided to franchisees (thus repeating his initial "mistake" of not using the Daigle e-mail provided in the notice of termination). Mr. Piotrowski reiterated the substance of his earlier calls, namely that he had closed his store pursuant to the notice of termination and was awaiting written communication from Mr. Daigle. Exhibit J.

Because Quiznos did not return any of their calls or the Help Desk e-mail, and having already turned away some lunch customers, Defendants decided to go ahead and open up the store, sometime around 11:30 a.m. They continued, unrelentingly and unsuccessfully, to call Mr. Daigle, the Help Desk and other Quiznos officials whose numbers they knew. No one ever returned any of their calls. Defendants' messages grew more and more desperate and aggressive. At one point, through a message Mr. Piotrowski left with someone other than Mr. Daigle, who then forwarded it to Daigle, Mr. Piotrowski advised Quiznos that Defendants were going to hold a press conference and complain about Quiznos' treatment of them.[4]

That, finally, seemed to get Mr. Daigle's attention. At what, by inference, seems to have been around 5:00 p.m. Defendants' time (eight hours after getting the notice of termination), Mr. Daigle finally sent Mr. Piotrowski an e-mail. Exhibit 25. It was not the stock e-mail inviting franchisees to open back up and qualify for a rescission of the termination if they passed an inspection. Instead, Mr. Daigle told Mr. Piotrowski that he, Daigle, had been informed about the threatened press conference, and that Quiznos would not tolerate any defamation or other harm. Daigle then wrote, "In case you are interested, following is the text of the e-mail you would have received had you taken the time to send me an e-mail as the support staff here suggested." Id. Mr. Daigle then inserted into the body of the e-mail the stock e-mail sent to every other inquiring terminated franchisee.

By the way, contrary to Mr. Daigle's claim, I find that no Quiznos support staff had ever suggested to Defendants that they should send an e-mail instead of call; indeed, that suggestion could never have been made because no one from Quiznos ever responded to any of Defendants' inquiries, until this response by Mr. Daigle. And of course the body of the notice of termination invites inquiries either by e-mail or telephone, without distinguishing between them.

In that same e-mail, Mr. Daigle invited Defendants to continue operating the store, but only to mitigate damages. As discussed below, this reference to mitigation makes no sense. If

[4] In later e-mails sent after Mr. Daigle had already decided not to give Defendants a chance to avoid the termination, Mr. Piotrowski also threatened to file a grievance against Mr. Daigle.

Quiznos terminated Defendants because Defendants breached the 6309 Agreement, then it is *Quiznos* that suffered damage and *Quiznos* that had a duty to mitigate those damages. Permitting, indeed encouraging, a breaching party to continue to operate under an agreement that has purportedly been terminated is not mitigating damages, it is waiving one's right to terminate.

In any event, Mr. Daigle not only did not invite a third-party inspection and rescission of the termination, two days later (on October 6, 2006) Quiznos commenced this action against Defendants, seeking liquidated damages. Mr. Daigle testified he treated Defendants in this singular way because he "was done with Mr. Piotrowski." When I asked him to explain to me, if terminating franchisees was never the intention of the field tests, why Defendants were not, in the end, given the same opportunity as everyone else to pass the inspection and get the termination rescinded, he testified that he did not know.

But it is quite clear to me what happened. Mr. Daigle got mad at Defendants because Mr. Piotrowski threatened to call a news conference, and Mr. Daigle decided at that instant that he would not afford Defendants the same opportunity he had afforded every other of the roughly 300 franchisees who were terminated. Indeed, Mr. Daigle testified that in his view, since all 300 of these franchisees were lawfully terminated, whether he chose to reinstate any one of them was entirely a matter of whether he wished to "accommodate" them. He decided not only not to accommodate Defendants, but to cause them to be sued for damages two days later.

Despite the commencement of this litigation, and for reasons no one at Quiznos could explain, except perhaps that the field operations folks simply did not know what the legal department had done, Quiznos sent a third-party inspector to Defendants' store later in October, and Defendants passed the inspection. Despite that passed inspection, Quiznos did not rescind its notice of termination or withdraw this lawsuit.

F. The Post-Termination Shadow Land

After being invited to "mitigate damages" by remaining open despite the termination, Defendants began what ended up being a 14-month period of operating their store in a Kafkaesque kind of shadow land between approved Quiznos franchisee and terminated franchisee/civil defendant. Quiznos continued to allow Defendants to buy food from its authorized supplier,[5] to use Quiznos' trade and service marks, and to hold themselves out as a Quiznos restaurant, but it cut off Defendants from the Help Line and from all other sources of official information. Quiznos even went so far as to physically bar Defendants from a regular marketing meeting they attempted to attend after the purported termination.

The evidence was mixed as to whether Quiznos also cut off Defendants from non-food supplies, such as paper products and plastic utensils. I find that, especially toward the end of this shadow period, Quiznos stopped supplying Defendants with many, though not all, of the non-food supplies necessary to operate the franchise, and in fact that Defendants were forced to buy many non-food products from other franchisees.

Most significantly, Quiznos removed Defendants' location from their 1-800 and on-line store locator. As a result, nearby customers interested in finding the Quiznos location closest to them were directed to other locations. This no doubt caused a serious drop in trade.

Perhaps the strangest element of this shadow existence was that Quiznos stopped taking its royalties and advertising fees. Before termination, Quiznos automatically withdrew those amounts from Defendants' operating account. Defendants continued to use the same operating account post-termination, but Quiznos stopped taking its royalties and fees (though during trial Quiznos'

[5] Actually, Quiznos cut off food sales to Defendants immediately after termination, but restored them a week later.

counsel complained about Defendants' failure to pay those royalties and fees). This failure to collect royalties and fees is a symptom of how profoundly confused Quiznos' legal department was about the nature of this shadow period. As mentioned above, if Quiznos' termination of Defendants had been lawful, it was Quiznos, not Defendants, who owed a duty to mitigate damages, and the single most apparent way to mitigate those damages was to collect royalties and advertising fees.

But of course Quiznos did not want to be seen as ratifying Defendants' post-termination operations, or worse still waiving its claim of a lawful termination, by collecting post-termination royalties and advertising fees. So we have this schizophrenic behavior by Quiznos in which it claims in a court-filed complaint that Defendants have breached the 6309 Agreement and that Quiznos has lawfully terminated it, and yet Quiznos invites Defendants to continue to operate and half-supplies them with the things they need to succeed. This ambiguous, confused, behavior was in some ways merely a continuation the ambiguous, confused manner in which Mr. Daigle conceived the whole non-termination termination program.

Because Quiznos stopped communicating with Defendants entirely, Defendants were not informed about any new developments, including new products. There was at least one new sandwich unveiled by Quiznos during this time, and Defendants were unable to sell it because they received no specifications for it, and were unable to advertise it because they were also getting no advertising materials. More importantly, Defendants were not getting any notices from Quiznos about recalled food product. It was this lack of communication that Mr. Piotrowski testified weighed heavily in Defendants' ultimate decision to close the store as a Quiznos store. There had been at least two general food recalls in the news, and Defendants were unwilling to run the risk that they might be selling food that had been recalled by Quiznos.

I find that as a direct result of this non-support from Quiznos, Defendants were forced to close their store as a Quiznos store in December 2007.

At this point let me address Quiznos' causation argument—that Defendants had never done well, that the store was on a downward decline from the moment they bought it, and that Quiznos' semi-cooperation in the shadow period had nothing to do with Defendants' decision to shut down the store as a Quiznos store.

First, as discussed below, this argument is legally unsound because I conclude Quiznos unlawfully terminated the 6309 Agreement, and as a result Defendants were not required to perform any of their post-termination obligations, except to mitigate *their* damages. That is, this is not a matter of causation at all, but a matter of acting reasonably in mitigation. I find that Defendants were eminently reasonable in accepting Quiznos' bizarre invitation to continue, and that if anything they went on too long and with too much hope in the ability of the product's sheer quality, and their own hard work, to translate into success. Indeed, they operated in this shadow state for almost twice as long as they operated as a full-blown Quiznos franchise.

But even as a matter of causation, I find that Defendants were forced to close their store by Quiznos' half-support. I reject Quiznos' interpretation of the economic evidence. It is true that this store had suffered steep and accelerating declines by virtually all measures of economic health (weekly and monthly adjusted and unadjusted gross revenue, weekly and monthly adjusted and unadjusted net revenue) during the period when Mr. Sterner owned it and Mr. Piotrowski operated it. Graphs 1, 2 and 3 to Defendants' economic expert's report, admitted as Exhibit 93. But in fact the picture started to turn around a little right before the sale to Defendants, and up until the purported termination the overall economic picture is that Defendants were generally able to stop the decline.

The way they did that was largely through their own hard work. They cut Mr. Sterner's wage overhead by working at the store themselves, full-time. Id. at Graph 5. They reduced the discounts. Id. at Graph 4. By these and other methods Defendants managed not only to continue the turn around that Sterner had begun, but actually to improve net revenues—not to Sterner's high but, on average, above the levels they inherited. Id. at Graph 3.

But the economics are only a part of this picture. Yes, Defendants may have been able to hobble along in shadow land indefinitely, pulling out modest wages and salaries and wondering what new sandwiches and food recalls they were missing. But the important point is that they were not legally obligated to do so. Quiznos terminated their franchise (unlawfully), and it was that termination that, in ordinary circumstances, would have been the proximate cause of Defendants' unmitigated losses. They cannot be punished for accepting Quiznos' shadow invitation to mitigate.

G. Out of the Shadows

Even after closing the store as a Quiznos store, Defendants still didn't give up. They remodeled, removing all Quiznos-identifying material, and reopened the store in May 2008 as the American Sub Sandwich Shop, selling sandwiches of their own design and buying food and paper products from their own independent suppliers. Defendants operated this store until August 2008, at which time they chose to close it, in no small part because of the increasing demands of this litigation. Zig Zag remains liable on the lease. And of course Zig Zag and Defendants remain liable on the SBA loan.

Again, I do not believe Defendants must prove they closed their new operation because of Quiznos; indeed, at this point Quiznos was officially out of the picture, shadow and all. The question, again, becomes mitigation, and as with their operation of the Quiznos store in the shadow period, I find that Defendants acted reasonably in attempting to mitigate their damages by operating a non-Quiznos sub shop in that same location.

H. Defendants' Disparagement of Quiznos

Quiznos introduced evidence that both before and after Defendants' purported termination in October 2006, Mr. Piotrowski posted numerous messages on a web site dedicated to having Quiznos franchisees air their grievances. I agree with Quiznos that many of these postings were disparaging, but I also find they had absolutely nothing whatsoever to do with Quiznos' decision to terminate Defendants' franchise. Moreover, as discussed in more detail below, Quiznos failed to prove that any disparagement so materially impaired their goodwill that they were justified in terminating Defendants because of it.

I. The Unreliability of the Mystery Shopper Test

I find that the mystery shopper test was completely unreliable, and certainly insufficient to be the basis of a decision as important as whether to terminate a franchisee. The test suffered from a host of design, operational and statistical defects, each one of which rendered it unreliable, and which in combination rendered it laughably unreliable.

First, the notion that these mystery shoppers could pull the melted cheese from the meat in anything close to a reproducible fashion, either as between the shoppers or even a given shopper as between different sandwiches, is preposterous. It doesn't take an expert to recognize that the way in which the cheese was placed on the meat, the random manner it happened to melt into the meat, and of course the particular practices of the mystery shopper as he/she attempted this impossible task, would have enormous variability, and that that variability directly and fatally infected the reliability of the test.

In fact, Mr. Manning's own second set of controlled tests—designed to confirm the test's reliability after complaints from field personnel—actually showed how unreliable this pulling-cheese-from-meat step really was, even under his ideal and controlled conditions, and with subjects well-versed in the protocol. His results show unequivocally that, despite the strict directives not to pull any meat off with the cheese, his test subjects did just that, about 70% of the time. Exhibit 83 (that portion marked Exhibit C). In fact, in one case (test #3) Mr. Manning's test subject pulled off 0.5 oz. of meat, more than enough to have caused an otherwise perfectly complying franchisee to test as non-compliant under the Daigle/Manning standards. Id.

Second, of course, by weighing the meat *after* it was cooked further in the au jus and toasted, Mr. Manning's test makes a host of assumptions about the amount the tested meat will shrink, and the variables that determine that shrinkage. Those variables, none of which Manning measured or otherwise attempted to control for, include the amount of fat in a given batch of prime rib, the amount of time the batch was pre-cooked, the time the meat was placed in the au jus,[6] the temperature of the au jus,[7] the vigor with which a particular sandwich-maker pressed on the meat to drain the au jus from it, the time a given sandwich spent under the toaster, and the temperature of the toaster. I agree with Defendants' cooking expert that these variables render the test's attempt to reverse engineer the original weights virtually worthless.

---

[6] Quiznos specifications in some places say the prime rib must be placed in the au jus for 20 seconds, but in other places say "at least 20 seconds." Both Defendants testified they often left the meat in the au jus for substantially longer than 20 seconds for customers who expressed a preference for well done meat.

[7] Quiznos' specifications allow a range from 160° to 180° for the temperature of the au jus. Of course, as several witnesses confirmed, including Defendants' cooking expert, placing cold meat into hot au jus will not only heat up the meat but also cool down the au jus. Thus, even if the au jus starts out at a temperature within specifications, it can quickly get out of spec. If the meat a mystery shopper happened to weigh was on a sandwich made during a slow period, the temperature of the au jus could have been be as high as 180°. But if the sandwich was the last in a long line made during a rush period, Defendants' expert testified a starting au jus temperature of 160° could drop as low as 130°.

These are not just theoretical problems thrown up by counsel and experts post hoc in the heat of litigation. Quiznos' own field personnel complained about the unreliability of the test. For example, Brian Savage, a Quiznos franchise support official, e-mailed Mr. Manning and reported that he and other team members conducted their own field tests and saw meat shrinkage of up 1.75 oz., which of course would obliterate the Daigle/Manning 4 oz. benchmark. Mr. Savage ended his e-mail with this sentence: "I could not, in good conscience, recommend a termination for anything I saw today." Exhibit 73.

One of Quiznos' mystery shoppers reported that after field tests in two locations resulted in weights below 4.5 oz., she asked the franchisees to make another sandwich and let her weigh the meat both before and after the au jus and toasting stages. She confirmed that the franchisees were using the required 5 oz., but that in both cases the meat tested at less than the 4.5 oz. after the au jus and toasting. She reported these results to her Quiznos supervisor, suggesting that perhaps the meat "just had a part of a body that had a lot of fat that melted away [during au jus and toasting]." Exhibit 43. The supervisor responded that this was "interesting," but that he did not have any instructions for her about how to deal with this problem. Id.

Quite apart from these substantial design and operational defects, which should have been apparent to anyone, and which became apparent in the field to the mystery shoppers themselves, the test simply fails as an exercise of statistical reliability. If the test were intended to be serious (which, as discussed above, it was not), Quiznos had a responsibility to consider whether it could make any reliable inferences from the single test of a single sandwich. There was no evidence about standard deviation, confidence intervals, statistical significance or any of the statistical inquiries one would expect if one party seriously intended to terminate the contract rights of another based on a single sample of a product made thousands of times during the life of a franchise. That is, even if I believed that the Manning test protocol could reliably reverse engineer the amount of meat put on the sandwich before the au jus and toasting phases, unless that protocol were demonstrably 100% reliable, these statistical inquiries are absolutely mandatory before Quiznos could confidently say that a franchisee was under-portioning based on a single sample.

Before I leave the area of statistics, let me also address the argument, made by Quiznos' counsel and some of the Quiznos witnesses, that the field test was proved reliable by the actual results of the test—Defendants being among a small number of franchisees found not above the 4.0 oz. level. In the first place, this argument is wrong as a matter of fact. Three hundred franchisees were sent the pretend termination notice. As I've already mentioned, that is more than 7% of all of Quiznos domestic franchisees, hardly de minimus. But more importantly, this argument that the test must be reliable because the results are distributed as expected misperceives the statistical issue. Expected outcomes are a necessary but not sufficient condition of reliability. As I indicated in my colloquy with counsel during closing arguments, the same overall outcomes could have been achieved by flipping a coin four times, and failing only those franchisees whose coin came up heads each of those four times. This would have produced a similar failure rate (6.25%), but of course the underlying "test" would be no test at all.

No discussion of the unreliability of the field tests would be complete without re-visiting the mystery shoppers' conclusions about whether any under-portioning was intentional. Remember, Defendants' meat tested at 4.0 oz., so they would never have been terminated but for Mr. Sanata's conclusion that the under-portioning was intentional. With no test forms, notes, or testimony, there is absolutely no basis for me to conclude, and there was no basis for Quiznos to have concluded, that Mr. Sanata's determination of intentionality was reliable.

Finally, it is worth mentioning that this field test was not only unreliable, it was both too strict and too forgiving for its real purpose. It was too strict because Subway's competing sandwich was made with 2 oz. of meat, so even test weights as low as 4 oz. would still meet the "more than twice the meat as Subway" tout, assuming *any* shrinkage during the au jus and toasting stages. It was too forgiving because it tested only the small Prime Rib Philly Cheesesteak, and not its larger versions.

II. THE CLAIMS AND COUNTERCLAIMS

Quiznos brings four claims for relief: 1) a claim for specific performance/injunctive relief, seeking an injunction directing Defendants to refrain from disparaging Quiznos; 2) a claim for breach of the 6309 Agreement, seeking liquidated damages; 3) a declaratory judgment claim, seeking a declaration that Quiznos lawfully terminated the 6309 Agreement and that Defendants must comply with their post-termination obligations; and 4) a claim for breach of the 8859 Agreement, seeking liquidated damages.[8]

After an amendment, and my ruling that their counterclaim for breach of the duty of good faith and fair dealing was not a stand-alone claim, Defendants assert two counterclaims: 1) breach of the 6309 Agreement, seeking damages; and 2) rescission of the 8859 Agreement, seeking a return of their $25,000 franchise fee for the 8859 store they never opened.

III. CONCLUSIONS OF LAW ON LIABILITY

For the reasons articulated below, I conclude that Quiznos has failed to prove any of its claims for relief, that Defendants have failed to prove their counterclaim for rescission of the 8859 Agreement, but that Defendants have proved their counterclaim for breach of the 6309 Agreement.

A. Quiznos' Claims

1. Quiznos' First Claim for Relief: Specific Performance/Injunction re Non-Disparagement

The short reason this claim fails is that, as discussed in Part III.A.2 below, Quiznos materially breached the 6309 Agreement by wrongfully terminating it, and as a result may not now attempt to enforce it. Quiznos' material breach excused Defendants' continued performance. *Kaiser v. Market Square Liquors, Inc.*, 992 P.2d 636, 641 (Colo. App. 1999).

In addition, although there is no doubt that many of Mr. Piotrowski's web postings did not "promote a good public image" of Quiznos as required by ¶ 11.1(b) of the 6309 Agreement, or that they were "disparage[ment]" within the meaning of the non-disparagement clause (¶ 9) of the Agreement and Conditional Consent to Transfer (part of Exhibit 2), in order to sustain their claim for injunctive relief Quiznos must also prove that 1) irreparable harm will result in the absence of an injunction; 2) the threatened injury outweighs the harm that the injunction might cause; and 3) the injunction will not disserve the public interest. *See, e.g.*, *Saint John's Church in Wilderness v. Scott*, 194 P.3d 475, 480 (Colo. App. 2008); *Langlois v. Board of County Comm'rs*, 78 P.3d 1154, 1158 (Colo. App. 2003). Here, Mr. Piotrowski made every one of these disparaging postings while Defendants were operating their Quiznos franchise, either pre-termination or in the post-termination shadow period. Exhibits S and T. There is absolutely no evidence that either Defendant disparaged Quiznos once they stopped operating the store as a Quiznos location in December 2007, and I therefore find and conclude that injunctive relief is simply not necessary to prevent any irreparable harm to Quiznos.

---

[8] This fourth claim for relief was not asserted in the original Complaint. It was added as part of Quiznos' "Amended Reply to First Amended Counterclaims," filed September 10, 2008.

2. Quiznos' Second Claim for Relief: Breach of the 6309 Agreement

Quiznos has failed to prove by a preponderance of the evidence that Defendants breached the 6309 Agreement. On the contrary, I conclude that Quiznos, not Defendants, breached the 6309 Agreement by wrongfully terminating Defendants.

As a preliminary matter, I conclude that by permitting Defendants to continue to operate as a Quiznos outlet, when the notice of termination and ¶ 18.7(b) of the 6309 Agreement specifically required Defendants to cease operating, Quiznos waived its right to terminate Defendants and to seek damages for breach, and is in any event estopped from making those claims.

Waiver is the intentional relinquishment of a known right, and is proved by the person asserting waiver by demonstrating that the other party acted inconsistently with an assertion of the right. *See, e.g., In re Marriage of Hill*, 166 P.3d 269, 273 (Colo. App. 2007). Quiznos was of course well aware of its right to require Defendants to cease operating upon termination, and indeed reminded Defendants of that requirement in the notice of termination itself. Even Defendants reminded Quiznos of it in their own telephone calls and e-mails. Quiznos proceeded by instructing Defendants they could continue to operate—that is, continue to use Quiznos' trademarks, service marks and goodwill, and continue representing itself as a Quiznos franchise—an instruction clearly inconsistent with Quiznos' claimed right to terminate Defendants.

Quiznos is also estopped from terminating Defendants. The elements of promissory estoppel are: 1) a promise which the maker should reasonably expect to induce reliance; 2) which in fact does induce detrimental reliance; and 3) in circumstances which would make it unjust not to enforce the promise. *Nelson v. Elway*, 908 P.2d 102, 110 (Colo. 1995). Defendants have proved each of these elements. Quiznos made a promise to Defendants that they could continue to operate, upon which they reasonably relied by continuing to operate to their detriment. The detriment is that Defendants spent 14 additional months of their lives in the shadow period, working 12-hour days six and seven days a week, when they were getting at best only half-hearted support from Quiznos. In my judgment, it would be profoundly unjust to allow Quiznos to recover damages for Defendants' alleged breach in making one sandwich with 0.5 oz. too little meat, when Quiznos was perfectly happy having Defendants continue to operate their shop as a Quiznos outlet for 14 additional months, but with absolutely no continued interest in the quality of Defendants' product.

Even if Quiznos has not waived this claim and is not estopped from asserting it, Quiznos has failed to prove that it had grounds to terminate Defendants. Paragraph 18.2(c) of the 6309 Agreement permits Quiznos to terminate Defendants only if, as pertinent here, Defendants engage "in conduct that, in the sole judgment of [Quiznos], materially impairs the goodwill associated with [Quiznos' trademarks and service marks]." Quiznos failed to prove by a preponderance of the evidence that Defendants engaged in any conduct that impaired Quiznos' goodwill at all, let alone materially impaired it.

Let me begin with the phrase "in the sole judgment of [Quiznos]" contained in ¶ 18.2(c). It is well-settled that language like this, purporting to give a contracting party limitless discretion in deciding whether facts exist upon which to base a termination decision, is necessarily overlain with an implied requirement that the discretion be exercised reasonably. *See, e.g., Omedelena v. Denver Options, Inc.*, 60 P.3d 717, 725-26 (Colo. App. 2003). Thus, the precise question under this claim is whether Quiznos has proved that it acted reasonably in determining that Defendants materially impaired Quiznos' goodwill. The answer to that question is a resounding no.

There was nothing reasonable about any of the actions Quiznos took against these Defendants, or the conclusions it drew about them. It was unreasonable for Quiznos to send out the notice of termination based on its palpably unreliable field test of a single sandwich on a single day. It was unreasonable for Quiznos to terminate Defendants on the basis of unsupported, unsupportable, and indeed false, allegations that any under-portioning was intentional. It was unreasonable for Quiznos not to anticipate that some franchisees, like Defendants, might respond to the notice of termination by calling instead of e-mailing, when the notice invited either. It was unreasonable for Quiznos not to anticipate that frantic franchisees, like Defendants, might not be able to get through by telephone. It was unreasonable for Quiznos not to return any of Defendants' telephone messages or their Help Line e-mail. It was unreasonable for Mr. Daigle, merely because he was offended at Defendants' threats to go public with the true nature of this Potemkin village field test, to decide that Defendants, and Defendants alone, would not receive his benevolence. It was unreasonable for Quiznos' legal department to cause this suit to be filed against Defendants two days later, without conducting any of the re-testing that Mr. Wooten ordered, and apparently without even knowing about that order for re-testing. It was unreasonable for Quiznos to maintain this claim after its own personnel determined that Defendants' alleged under-portioning was "Not 100% intentional," and after Defendants passed the inspection done by independent third-parties.

It was, in the larger context of what happened in this case, unreasonable for Quiznos to put its franchisees' livelihoods at risk so cavalierly, and on the basis of such flimsy and palpably unreliable evidence, and then stubbornly to single out Defendants in an instant of in-house pique.

Quiznos alternatively argues that it had a right to terminate Defendants because of Defendants' disparagement. This argument also fails. Quiznos' purported termination of Defendants had nothing whatever to do with any disparagement. Once Defendants were wrongfully terminated, they had no continuing duty to refrain from disparaging Quiznos, so this claim fails as a matter of law to the extent it is based on any post-termination disparagement.

In any event, Quiznos has not proved that any of Defendants' disparagement *materially* impaired Quiznos' goodwill, as is required for termination under ¶ 18.2(c). Indeed, Quiznos has not proved that its goodwill was damaged at all by Mr. Piotrowski's disparaging postings. Quiznos did not produce a single customer, prospective franchisee, or any other non-Quiznos witness to prove that the disparagement impaired Quiznos' goodwill. In fact, the evidence was not at all clear that the website on which these disparaging remarks were posted was even accessible by the public.

3. Quiznos' Third Claim for Relief: Declaratory Judgment that Quiznos Lawfully Terminated the 6309 Agreement

For all of the reasons I have already articulated in rejecting Quiznos' claim for breach, I also reject its claim that it lawfully terminated the 6309 Agreement. It did not lawfully terminate that Agreement. It breached it by wrongfully terminating Defendants.

4. Quiznos' Fourth Claim for Relief: Rescission of the 8859 Agreement

Quiznos has failed to prove that Defendants violated the 8859 Agreement by failing to begin operations under that Agreement within 12 months after its execution, since Quiznos waived that requirement by waiting two-and-a-half years after its expiration to assert this claim. It also waived that requirement by specifically notifying Defendants they need not worry about the 12-month deadline, without following up and establishing a new deadline. Moreover, this claim also fails because Quiznos has not proved any damages. I do, conclude, however, that the parties terminated the 8859 Agreement by their mutual abandonment of it, and that the proper remedy is simply for Quiznos to retain the $25,000 franchise fee Defendants paid under that Agreement.

As discussed in Part I.B above, in April 2006, some four months after the 12-month deadline had already expired, Defendants expressed concern to Quiznos about the deadline, and

Quiznos informed them that they need not worry about it. Exhibit 27. As also discussed above, no one from Quiznos ever contacted Defendants again to re-set that already expired deadline. Indeed, Quiznos never took any action to assert its rights under that deadline until long after it brought this action, and then only in response to Defendants' counterclaims for rescission of the 8859 Agreement.

I conclude that these actions and inactions by Quiznos amounted to a waiver of their right to terminate the 8859 Agreement for Defendants' failure to begin operations in 12 months.

Even if it had not waived its right to rescind the 8859 Agreement, Quiznos is not entitled to the liquidated damages it seeks under ¶ 21.3 of the Agreement. First, it is important to recognize that the provision in which this 12-month deadline is contained, ¶ 6.9, does not itself provide for any remedy for its breach. Second, the general remedies provision, at ¶ 21.3, provides that "the court will have the right to award any relief which it deems proper," with some subsequent limitations not pertinent to this issue. I certainly do not think it "proper" to award Quiznos anything other than retention of its $25,000 franchise fee for terminating this agreement, when Quiznos never became obligated for any operational assistance and in fact, save its unsuccessful attempts to help Defendants find a location, is not out one penny.

This conclusion is reinforced by the plain and unambiguous language of the very liquidated damage provision on which Quiznos relies. That provision, also in ¶ 21.3, states:

> [I]f this Agreement is terminated because of a Franchisee default, Franchisee shall be liable to Franchisor for a lump sum amount equal to the net present value of the Royalties and Marketing and Promotion Fees that would have become due following termination of this Agreement for the period this Agreement would have remained in effect but for the Franchisee's default. *Royalties and Marketing and Promotion Fees for purposes of this Section shall be calculated based on the Restaurant's average monthly Gross Sales for the twelve (12) months preceding the termination date.*

8859 Agreement, ¶ 21.3 (emphasis added). That is, these liquidated damages are to be based exclusively on historical royalties and fees, and of course because Defendants never opened a restaurant under the 8859 Agreement there are no historical royalties and fees, and the measure of these damages is therefore zero.

What I find really happened with the 8859 Agreement is that both parties, by their inaction—Quiznos in waiving the 12-month deadline then never re-setting a new one, and Defendants in never opening the 8859 location—mutually abandoned it. Quiznos is therefore entitled to retain the $25,000 franchise fee, but is not entitled to any other damages.

B. Defendants' Counterclaims

1. Defendants' Counterclaim for Breach of the 6309 Agreement

For all the reasons I have already articulated in concluding that Defendants did not breach the 6309 Agreement, I conclude that Quiznos did breach it by wrongfully terminating Defendants. I also conclude that that breach was material and substantial. A breach doesn't get more material or substantial than wrongfully terminating a contract. I address damages in Part IV below.

2. Defendants' Counterclaim for Rescission of the 8859 Agreement

For all the reasons I have already articulated in concluding that Defendants and Quiznos mutually abandoned the 8859 Agreement, I conclude that Defendants have failed to prove that they are entitled to rescission of that Agreement.

IV. DEFENDANTS' DAMAGES FOR QUIZNOS' BREACH OF THE 6309 AGREEMENT

I conclude that Defendants have proved their entitlement to rescissional-type damages as a remedy for Quiznos' wrongful termination of the 6309 Agreement, and that the proper amount of those damages is $349,797.00, plus costs, fees, and post-judgment interest at the contract rate of 24%.

A. The Proper Measure of Damages

Ordinarily, contract damages should be based on the benefit-of-the-bargain measure, that is, they should restore the claimant to the position he would have been in had the other party not breached. *See, e.g.*, *Goodyear Tire & Rubber Co. v. Holmes*, 193 P.3d 821, 826 (Colo. 2008).

However, it is also well-settled in Colorado that when a breach is substantial, the injury irreparable and ordinary contract damages inadequate, difficult or impossible to assess, rescissional damages may be awarded, that is, damages that do not just return the parties to the moment before the breach, but return them to the moment before the contract was even entered into. *EarthInfo, Inc. v. Hydrosphere Res. Consult., Inc.* 900 P.2d 113, 118 (Colo. 1995); *Ralston Oil & Gas Co. v. July Corp.*, 719 P.2d 334. 339 (Colo. App. 1985).

Here, Quiznos' breach was of course substantial, as I have already concluded. For many reasons peculiar to the facts of this case, I also conclude that the injuries to Defendants were irreparable, that ordinary contract damages are impossible or difficult to assess, and that in any event such damages would be inadequate.

First, and perhaps most significantly, Quiznos wrongfully terminated the 6309 Agreement after Defendants had only operated their store for a little over eight months. This hardly gave Defendants the time they needed to establish a reliable economic baseline on which to ground traditional contract damages, and has made the calculation of those traditional damages difficult if not impossible. Indeed, the traditional rule had been that lost profits were not recoverable at all for a "new business," though the modern rule in the majority of states, including Colorado, is that such damages may be recovered if they can be proved with reasonable certainty. *International Tech.*

Instr., Inc. v. Engineering Meas. Co., 678 P.2d 558 (Colo. 1983). See generally ROBERT L. DUNN, 1 RECOVERY OF DAMAGES FOR LOST PROFITS § 4.3 (6th ed., 2005). But of course when, as here, the newness of the business makes it difficult to establish traditional damages, that difficulty is something I should, and indeed must, take into consideration in deciding whether rescissional damages are more appropriate.

I recognize that Defendants' damage expert expressed an alternate opinion on the amount of traditional damages, but that opinion was fraught with all kinds of speculation endemic to the reality that Defendants did not operate the store long enough for any calculation of traditional contract damages to be sufficiently certain.

The short period Defendants operated pre-termination also means that rescissional damages will not unduly distort the parties' expectations by winding things back for a substantially longer period than would be the case if ordinary contract damages were awarded. It is precisely because Quiznos wrongfully terminated Defendants' operations so soon that, in my judgment, it is more appropriate to try to return Defendants to the moment before they entered into the 6309 Agreement, rather than to the moment eight months later when Quiznos wrongfully terminated it.

Second, Defendants' attempt to mitigate their damages by continuing to operate the store post-termination, with Quiznos' permission and invitation, was itself interfered with by Quiznos' failure to support the store fully. It seems hardly just, and certainly inadequate, to punish Defendants with speculative mitigation deductions from a traditional damage computation, when Quiznos' lack of support was just a schizophrenic continuation of their wrongful termination. As Defendants' damages expert put it, Quiznos, both through their wrongful termination and then through their failure to support Defendants' attempts at mitigation, ended up destroying

Defendants' business, not in one fell swoop but over an agonizing period of 14 months of slow kill. I agree with this description and conclusion.

Traditional damages are also inadequate because the parties contractually agreed to limit Defendants' right to lost profits to one year's worth of income, as measured by the 12 months immediately preceding the breach. 6309 Agreement ¶ 21.3. Here, Defendants did not have 12 months of operations, and in fact in their eight months they reported a taxable loss. So any traditional measure of contract damages would not include lost profits, which in a business case is often the most significant component of the traditional measure.

I can see that in more ordinary circumstances a breaching party like Quiznos might legitimately object to a court considering a contractual damage limitation like this in making the decision of whether to award rescissional or traditional damages. After all, this limitation was part of the parties' bargain. Rescissional damages should not be a way to end-run damage limitations to which contracting parties have agreed.

But these are not ordinary circumstances. The breaching party here, through its own refusal to support Defendants' mitigation efforts, actually caused the failure of the business and therefore created the very circumstances in which Defendants could not continue the business and perhaps achieve a 12-month track record showing a taxable gain. Even more importantly, the actual language of this limitation is non-exclusive. Paragraph ¶ 21.3 recognizes that only the "lost earnings and profits" component of damages is to be limited, and clothes the court with virtually unlimited authority to award "any relief which it deems proper in the circumstances." That is, a rescissional award is itself within the contemplation of the parties' bargain.

For all of these reasons, I conclude that damages based on a rescission theory are the appropriate measure of damages in this case. Let me now turn to the amount of those damages.

B. The Amount of Rescissional Damages

Defendants' damages expert calculated rescissional damages in four different categories: 1) recovery of Defendants' direct investment in the restaurant, less their income from it; 2) recovery of their lost opportunity to invest in alternatives; 3) their liability on the real estate lease; and 4) a category the expert calls "estimated absorbed management compensation." Let me address each of these categories in order.

1. Direct Investments

I agree with Defendants' expert's rather straightforward calculations that the amount of these direct investments is $190,020. This amount consists of Defendants' equity investments, advances, loans (including the SBA loan) and net operating loss (which was a gain because of the estimated liquidation value of the assets), less all the income Defendants derived from the operation of the restaurant. It does not include interest.

2. Lost Opportunity

I also agree with Defendants' expert that Quiznos should pay Defendants what amounts to interest on their net direct investment, or what the expert called "lost alternative investment opportunities." I disagree, however, with the expert's use of the statutory interest rate of 8%, since the parties agreed in their contract that "the defaulting party will pay the prevailing party . . . all damages . . . plus interest at the lesser of two percent (2%) per month or the highest commercial contract rate allowable by law accruing from the date of default." 6309 Agreement ¶ 23.6. Since the maximum allowable interest in Colorado for non-consumer transactions is 45% per annum, § 5-12-103(1), this contract provision means the parties have agreed to interest, both pre-judgment and post-judgment, at an annual rate of 24%.

When I use 24% instead of 8% in the calculations contained in Exhibit S3 to the expert's supplemental report (Exhibit 95), I get a total for this item of $39,777.

3. Lease

I agree with Defendants' expert that Defendants are entitled to be compensated for their liability on the real estate lease for the Coopersburg premises, but disagree with the expert's calculation of that liability. It is true that the lease is now in default, that the landlord has accelerated the payments due over the lease term, and that that amount equals, according to the landlord's own testimony, $260,096. But this figure does not account for the landlord's duty to mitigate by re-letting the premises, a duty I presume he has under Pennsylvania law, and which in any event he has under the express terms of the lease. Exhibit 8, ¶ 14(d)(1).

Quantifying this mitigation is very difficult. On the one hand, I am almost certain this space will not remain un-rented for the next six years (the balance of the lease term). On the other hand, I believed Defendants' testimony that they have been trying to sub-let the premises since August 2008, to no avail. The landlord would not hazard a guess about how long this space might remain vacant, but did testify that he has a larger space in the same area that has remained vacant for more than a year. I also cannot help to take notice of the generally weak state of the economy, not to mention the specific area of the rust belt—central Pennsylvania's Lehigh valley—in which this location sits. Taking all these facts into consideration, my most reasoned estimate about how much Defendants will owe to their landlord, after deducting for mitigation, is $120,000.

Before I take up the next category of damages, let me address the fact that, unlike with the SBA loan, Defendants never guaranteed the lease, and therefore only Zig Zag is liable on it. Given that Zig Zag was created for the sole purpose of operating the Quiznos restaurant, that Mr. Piotrowski and Ms. Blickman are its only members and are married to each other, and that all the other direct contributions seem to have been made by Defendants individually, I think it appropriate to disregard the corporate form at least for the purposes of this damage award. Of course, I am not addressing, or even speculating about, the question of whether the landlord could prevail on a piercing claim. I am simply saying that for purposes of awarding these rescissional damages, I will make the award to all three Defendants without distinguishing between them, much as I have not distinguished between how much of the direct investments were made by Mr. Piotrowski and how much by Ms. Blickman.

4. Absorbed Management Compensation

I understand this category to be the labor analog of lost investment opportunity, that is, this item is intended to repay Defendants for the difference between what they pulled out in salaries and wages on the one hand and what they *could* have earned doing similar work for someone else. But unlike the lost investment opportunity item, which is just a fancy phrase for interest on their investment, I do not believe absorbed management compensation is an appropriate item of rescissional damage. Defendants made a choice to invest their sweat equity in this business, instead of earning more in the short-run working for someone else. I think it would be unfair to require Quiznos to pay for that choice.

Moreover, it seems to me that this item conflates rescission with the traditional measure of contract damages. Under the rescission measure I have adopted, Defendants' investment in this business must be unwound, and an amount awarded today to represent that unwinding. Awarding Defendants the difference between the value of their labor as they chose to spend it and the value of how they could have spent it smacks of a benefit-of-the-bargain measure, not rescission.

I will therefore disallow the $18,600 entry the expert attributes to this item. Exhibit SU1 to Exhibit 96.

5. Conclusion on Rescissional Damages

I conclude that Defendants have suffered the following items of rescissional damage:

Item	Amount
Recovery of Direct Investments	$190,020
Interest (lost investment opportunity)	39,777
Costs of Default on Lease	120,000
Total:	$349,797

C. FEES AND COSTS

The 6309 Agreement has an attorney fees clause that requires the "party in default" to pay the "prevailing party" all the attorney fees and costs "incurred by the prevailing party in any legal action or other proceeding as a result of such default . . . ." Exhibit 2, ¶ 23.6. Of course, even in the absence of this provision, the prevailing party is entitled to costs under C.R.C.P. 54(d).

Under contractual fee-shifting provisions such as the one here, the prevailing party is the party in whose favor a decision on contractual liability is rendered. *See, e.g., Dennis I. Spencer Contract., Inc. v. City of Aurora*, 994 P.2d 326, 332 (Colo. 1994); *Coe v. Crady Davis Corp.*, 60 P.3d 794,796 (Colo. App. 2002). Here, I have concluded that Quiznos, not Defendants, breached the 6309 Franchise Agreement. Quiznos is therefore the "defaulting party" and Defendants the "prevailing parties" within the meaning of ¶ 23.6 of the 6309 Agreement.

The 8859 Agreement has an identical fee-shifting provision, but because the parties mutually abandoned that Agreement, and both of their claims under that Agreement have failed, I conclude that neither party is the "prevailing party" with respect to the claims under the 8859 Agreement.

D. Interest

As discussed in Part IV.A above, the parties agreed in the 6309 Agreement to interest at the rate of 24%. Defendants are therefore entitled, in addition to the pre-judgment interest at this rate, which I have already awarded, to post-judgment interest at this same rate.

V. CONCLUSION

1. All of Quiznos' claims against Defendants are HEREBY DISMISSED WITH PREJUDICE.

2. Defendants' counterclaim for rescission of the 8859 Agreement is HEREBY DISMISSED WITH PREJUDICE.

3. JUDGMENT HEREBY ENTERS in favor of Defendants, Zig Zag Restaurant, LLC, Ellen Blickman and Richard Piotrowski, and against Plaintiff Quiznos Franchising II, LLC, on Defendants' counterclaim for breach of the 6309 Agreement, in the amount of $349,797.00, plus fees, costs and post-judgment interest at the contract rate of 24% per annum.

4. Defendants shall file a bill of costs and a motion and affidavit for fees by January 26, 2009, and those filings shall be briefed in the ordinary course.

5. Any motions under C.R.C.P. 59 shall also be filed by January 26, 2009.

DONE THIS 31ST DAY OF DECEMBER, 2008.

BY THE COURT:

Morris B. Hoffman
District Court Judge

cc: All counsel