

SUPREME COURT OF NOVA SCOTIA

Citation: *Body Shop Canada Ltd. v. Dawn Carson Enterprises Ltd.*,
2014 NSSC 239

Date: 20140627

Docket: Hfx No. 306885

Registry: Halifax

Between:

The Body Shop Canada Limited

Plaintiff

v.

Dawn Carson Enterprises Limited and Dawn Carson

Defendants

v.

OPB Realty (Halifax Center) Inc. and 20Vic Management Inc.

Third Parties

Decision

Judge: The Honourable Justice Gerald R. P. Moir

Heard: April 15, 16, 17, 22, December 12, 16, 17, 18, and 19, 2013

**Final Written
Submissions:** January 24, 2014

Counsel: Geoffrey A. Saunders, for the plaintiff
Kevin A. MacDonald, for the defendants
Jeffrey Aucoin and Chase Barlet, for the third parties

Moir J.:

Introduction

[1] A "Body Shop" is a retailer of soaps, cosmetics, and such products. The business was founded in England. It operated in Canada through a franchisee who owned some shops directly and subfranchised others. Eventually, the Body Shop business was sold to a large American retailer, L'Oréal.

[2] Dawn Carson Enterprises Limited is named for its owner. She established Body Shop franchises in Halifax, eventually one at the Halifax Shopping Centre in the west end and the other at the Parklane mall on Spring Garden Road.

[3] The Body Shop Canada Limited was the Canadian franchisee. Ms. Carson's company was its subfranchisee for the two shops. Body Shop Canada leased the shops from mall landlords and subleased them to Dawn Carson Enterprises. Ms. Carson guaranteed the franchise agreements and the subleases.

[4] The landlord of the Halifax Shopping Centre was OPB Realty (Halifax Center) Inc. OPB stands for Ontario Pension Board. The mall manager was 20Vic Management Inc.

[5] Rents paid between 1999 and 2008 for the Halifax Shopping Centre shop were audited on behalf of OPB. The auditors found that the subtenant, Dawn Carson Enterprises, had under-reported its gross revenue each year, and consequently underpaid percentage rent. The tenant owed arrears of percentage rent plus taxes, interest, and audit expenses.

[6] OPB sued Body Shop Canada and Dawn Carson Enterprises. Body Shop Canada settled the suit for \$156,232. It terminated the subfranchise agreement and sued Dawn Carson Enterprises on the sublease and Ms. Carson on the guarantee.

[7] Ms. Carson and her company counterclaimed, and they made third party claims against OPB and 20Vic Management. The pleadings reference breach of the subfranchise agreement against the plaintiff and tortious interference against the plaintiff and the third parties. Other claims against the third parties were dismissed as a result of Justice Bourgeois' decision in *Body Shop Canada Ltd. v.*

Dawn Carson Enterprises Ltd., 2010 NSSC 25. Nevertheless, the pretrial brief refers to "Breach of Contract, Breach of Fiduciary Duty, Equitable Fraud, Tortious Interference, Breach of Implied Duty of Good Faith and Fair Dealing, Economic Duress, Extortion, etc."

[8] Dawn Carson Enterprises conceded that it understated gross revenue, and underpaid percentage rent. The concession was made in April of 2008, after the audit. At that time, and ever since, Ms. Carson maintained that the understatement resulted from innocent error. She repeated that position when she testified. The position is not credible.

[9] Ms. Carson says she followed the method for calculating gross revenue taught to her by an accountant in the 1980s, which method may not have been applied by the auditors. She also explains that the understatement resulted from her, or her staff, inadvertently twice subtracting amounts properly subtracted once to calculate gross revenue.

[10] The first part of the explanation does not make sense. Calculation of gross revenue in a retail shop is not an esoteric exercise. One ascertains total receipts,

which were clearly shown on Dawn Carson Enterprises' source documents and which were meticulously recorded by staff under Ms. Carson. One subtracts sales taxes collected and separately held for remittance, which were also clearly shown and meticulously recorded. And, one makes some lesser adjustments, such as for returns, depending on one's definition of gross revenue.

[11] This simple process leaves no room for the huge differences between gross revenues reported by Ms. Carson to the landlord and the actual gross revenues from the Halifax Shopping Centre Body Shop.

[12] The second part of the explanation is not credible. Barbara Foote joined Ms. Carson's company in 1994 and, by 1998, she was in charge of bookkeeping and accounts. The evidence shows that her work was meticulous. Among other things, she took the cash amount daily from source documents and transposed the information onto a spreadsheet, which turned into sales reports that she submitted to the company's chartered accountants each month, who used them in the preparation of annual financial statements.

[13] Ms. Foote moved to Washington, D.C. in 2007, but she supervised the work of her successor.

[14] There can be no doubt that Ms. Foote and her successor made accurate adjustments to recorded cash in reaching "net sales" by adjusting for sales taxes, gift certificates redeemed against gift certificates sold, refunds, and exchanges. These and other results of her financial work were delivered to the company accountants, but not to the landlords.

[15] Although she was not the person directly responsible for financial recording, Ms. Carson kept to herself the reporting of gross revenues to the landlords. Ms. Foote, whose evidence I accept, said that her instructions were to refer representatives of the landlord to Ms. Carson when they were looking for information on gross revenues.

[16] Ms. Foote's net sales were roughly equivalent to the lease's gross revenues:

... all of the gross receipts and revenues of every nature and kind with respect to all business conducted by any means at, in, upon, through or from the store ... excluding only the amount of refunds on sales previously included and provincial sales taxes to the extent separately recorded and remitted.

Under instructions from Ms. Carson, Ms. Foote gave the monthly net sales figures to Ms. Carson for preparation of the revenue reports to the landlords. No staff member subtracted refunds and provincial sales tax a second time because they were not involved beyond the meticulously correct statements of net sales.

[17] Ms. Carson did not "inadvertently" subtract the taxes, returns, or other permitted credits, a second time. Ms. Foote testified, and I find, that Ms. Carson regularly sought confirmation that the expenses had been backed out of net sales. I find she regularly received that assurance.

[18] Further, the discrepancy between gross revenue reported to the Halifax Shopping Centre landlord by Ms. Carson monthly and annually for almost a decade and actual gross revenue was so great that doubling the permitted credits does not come close to explaining the discrepancy.

[19] Just as Ms. Carson's explanations made no sense, her statements of gross revenue themselves made no sense. Ms. Carson did not explain how she reached the numbers she reported to the landlord. We do not know the method putatively taught to her in the 1980s.

[20] These introductory reasons state my most basic findings after two weeks of trial and introduction of thousands of documents. Acceptance of a simple truth unravels all of Ms. Carson's defences and claims. She caused rents to go unpaid to the Halifax Shopping Centre landlord by understating revenues month in and month out, year in and year out.

Ms. Carson's Body Shops

[21] Ms. Carson encountered Body Shop while travelling in Europe in the early 1980s. When she returned to Canada in 1983, she discussed the possibility of opening a shop. She called Body Shop in the United Kingdom and was referred to a numbered Canadian company, who held the franchise here.

[22] In March of 1984, Ms. Carson opened a shop in Spring Garden Place. She says there was nothing like it in Nova Scotia, where cosmetics had only been offered in pharmacies and grocery stores. Also, she was attracted to what she described as "incredibly solid values" such as charitable work, treatment of animals, fair trade, and environmental protection.

[23] The Body Shop values led Ms. Carson's shops to support Phoenix House, which provides housing and counselling for young people. Staff provided volunteer services on company time.

[24] The Spring Garden Place shop moved across the road to the Parklane shopping mall in 1984. Ms. Carson handled the negotiations for a lease and sublease. The franchisor signed off on the negotiated lease, and her company took the sublease.

[25] About the same time as the move to Parklane, Ms. Carson opened a second shop. It started out in the Bayers Road Shopping Centre. Once again, Ms. Carson negotiated the lease and sublease, with the Canadian franchisee's cooperation.

Percentage Rate Under the Halifax Shopping Centre Lease

[26] In the late 1990s, Bayers Road Shopping Centre was becoming tired, and the nearby Halifax Shopping Centre was being renovated. Ms. Carson's shop moved there in 1998.

[27] The lease is a standard form for Halifax Shopping Centre tenants. The landlord is OPB Realty (Halifax Center) Inc. and the tenant is the Canadian franchisee. It is dated in 1997 for a term from March 15, 1998 to March 31, 2008. 20Vic Management Inc. is defined as "manager".

[28] The lease starts with a general provision expressly imposing good faith obligations and confirming that the lease is absolutely net. Section 1.2 is titled "Basic Principles of the Contract", and it reads:

This is a lease as well as a business contract. The parties expect and intend that each will act in good faith and in a commercially reasonable manner in accordance with this agreement in enjoying and performing the rights and obligations of each party as set forth in this agreement. It is intended that this lease be an absolutely net lease for Landlord and that rent be received by Landlord free of any cost or obligation concerning the Store or the Project unless specified in this lease. Each provision of this agreement applicable to each party although not expressed as a covenant, shall be construed to be a covenant of such party for all purposes.

[29] A schedule to the lease defines "rent" as basic rent, percentage rent, and additional rent. Section 3.1 requires payment of basic rent monthly, and an appendix incorporated by both s. 3.1 and the definition of "basic rent" provides for \$30 a square foot.

[30] The percentage rent kicks in only when six percent of gross revenue exceeds the amount paid for basic rent in a lease year (April to March). The liability is imposed by s. 3.2, which reads:

Tenant shall pay to Landlord in each lease year, further rent equal to the amount, if any, by which the percentage specified in key data item 11 of Gross Revenue in such lease year exceeds Basic Rent for such lease year. Percentage Rent shall be payable by monthly instalments in arrears, within 15 days after the last day of each month in each lease year. The amount of each instalment shall be calculated on a cumulative basis in each lease year by computing the aggregate Gross Revenue for such lease year up to and including the month preceding the month in which such instalment is due, applying the percentage referred to above for such lease year, and deducting the aggregate of instalments payable on account of Basic Rent for such lease year up to and including the instalment payable for such preceding month, and the aggregate of previous instalments of Percentage Rent payable for such lease year, all based upon the monthly statements of Gross Revenue referred to in section 3.6.1, and subject to subsequent adjustment under section 3.6.2.

The "key data item 11" is in the appendix. It reads "Percentage Rent: 6% of Gross Revenue, less Basic Rent". Gross revenue is defined in a schedule:

"Gross Revenue" means all of the gross receipts and revenues of every nature and kind with respect to all business conducted by any means at, in, upon, through or from the Store and any Competing Business and, whether at wholesale or retail, whether for cash, credit, exchange of merchandise or other consideration and whether by Tenant or any other person conducting business at, in, upon, through or from the Store and any Competing Business including every subtenant, franchisee or licensee; and including the selling price of all merchandise and services sold or delivered and entertainment provided by machines, including vending machines and machines operated by coins, credit cards or otherwise; excluding only the amount of refunds on sales previously included and provincial sales taxes to the extent separately recorded and remitted. Each sale shall be treated as a sale for the full price (including all finance charges) at the time such sale is made, regardless of when or if Tenant receives payment.

[31] Section 3.6 concerns both reporting and method of payment of percentage rent. Section 3.6(2) requires payment of percentage rent in any month in which six percent of gross revenue exceeds basic rent, and provides for an adjustment at the end of the lease year by which the landlord refunds an excess of payments over rent or the tenant pays an excess of rent over actual payments. Usually, liability to pay percentage rent would not accrue until the binge buying that has become Canadian Christmas, i.e. in the months of November and December.

[32] Section 3.6(1) of the lease requires the tenant to accurately report its gross revenue each month and to provide an audited statement yearly:

Within 15 days after the last day of each month of every lease year, Tenant shall deliver to Landlord a statement in writing certified by Tenant and accurately setting forth Gross Revenue for such month. Within 60 days after the last day of

each lease year, Tenant shall deliver to Landlord a statement in writing, certified by Tenant and audited by an independent chartered accountant who is acceptable to Landlord, accurately setting forth and with reasonable detail and particulars, Gross Revenue for each month in such lease year. The statement shall include a certification by such accountant that Gross Revenue has been calculated in accordance with the definition of that term in this lease.

It appears that the requirement for annual audited statements was ignored or waived.

[33] The lease also required the tenant to keep records for ascertaining percentage rent. (Ms. Carson argues that this provision also extinguishes the tenant's liability to pay percentage rent that accrued more than eighteen months before the latest lease year, a subject I shall take up later.) The requirement is in section 3.7:

For the purpose of ascertaining the Percentage Rent, Tenant shall prepare and keep at Tenant's head office in Canada for a period of not less than 18 months following each lease year, adequate records for such lease year which shall show inventories and receipts of merchandise at the Store and any Competing Business and daily receipts from all sales and other transactions, the proceeds of which are to be included in Gross Revenue. Tenant shall record at the time of sale, in the presence of the customer, all receipts from sales or other transactions whether for cash or credit in a computerized or electronic cash register or in cash registers having a cumulative total which shall be sealed in a manner approved by Landlord, and having such other features as shall be approved by Landlord. Such records shall include such sales and inventory records which would normally be examined by a licensed independent public accountant pursuant to generally accepted auditing standards in performing an audit of the entire business affairs and sales by any person at, in, upon through or from the Store and any Competing Business.

[34] Section 3.8 allows the landlord to audit the percentage rent after a statement is delivered and it requires the tenant to pay any outstanding rent immediately.

The landlord bears the cost of the audit unless the tenant's records are inadequate or a variation of more than two percent is discovered. The section reads:

At any reasonable time after the delivery or failure to deliver to Landlord any statement referred to in section 3.6.1, Landlord shall have the right by its officers and auditors to cause a complete audit to be made of Tenant's entire business affairs and records relating to the Store and any Competing Business and to examine such business affairs and records to confirm or establish the amount of the Percentage Rent for the period to which such statement relates. If the records maintained by Tenant for the period under review are not made available to Landlord or are inadequate to permit the determination of Gross Revenue for such period, Landlord may estimate the Gross Revenue for such period and such estimate shall be deemed to be the Gross Revenue for such period. The cost of each such audit and examination shall be borne by Landlord unless Tenant fails to deliver any statement or such audit and examination discloses a variation in excess of 2% of the amount of the statement with respect to which such examination is conducted in either of which events such cost shall be borne by Tenant. Any additional Percentage Rent found to be due and owing to Landlord as a result of an audit or examination shall be paid immediately.

Halifax Shopping Centre Sublease

[35] This document was executed by Body Shop Canada and Dawn Carson

Enterprises in September of 2006 in connection with a new subfranchise

agreement after L'Oréal bought the international Body Shop business and after a

class action by Body Shop franchisees was settled. Body Shop Canada sublet the then Body Shop premises in the Halifax Shopping Centre to Ms. Carson's company.

[36] Ms. Carson's company promised to pay the rent required to be paid by Body Shop to OPB including the percentage rent: s. 2(a). It also promised to "observe and perform all of the other terms, covenants and conditions on the part of BSL": s. 2(b). Rents were to be paid by Ms. Carson's company directly to the landlord, and the company agreed to indemnify Body Shop Canada and others: s. 2(f) and s. 11.

[37] At the time of the new subfranchise and sublease, Ms. Carson signed and delivered a guarantee under seal. The guarantee is in favour of the international franchisor and Body Shop Canada. The "guaranteed obligations" included all liabilities of Dawn Carson Enterprises under "agreements", which included the sublease.

Underpayment of Percentage Rent

[38] Mr. James Hedrich is experienced in the shopping centre industry. He is the vice-president for leasing with 20Vic, a position he was appointed to eight years ago after more than a decade with the company.

[39] I find Mr. Hedrich is an able and straightforward business person. I found him to be a straightforward witness. I accept his evidence.

[40] In September of 2007, Mr. Hedrich met in Toronto with Mr. Michael Porter of the new international Body Shop under L'Oréal, and another person who was assisting it with leasing. The purpose of the meeting was to continue negotiations on various Body Shop leases coming up for renewal in malls managed by 20Vic. One of those was the Dawn Carson Body Shop in the Halifax Shopping Centre.

[41] 20Vic had made an offer for a new lease. In consultation with Ms. Carson, the international Body Shop was preparing a counteroffer. The amount of basic rent was emerging as the most contentious issue.

[42] Mr. Hedrich came to the meeting with pertinent information, including the sales volumes of the various Body Shop tenants. He remarked that he did not understand why sales were so low at the Halifax Shopping Centre shop. When Mr. Hedrich showed Mr. Porter the figures he had for gross revenue, Mr. Porter replied that he thought Body Shop's figures were substantially higher than that.

[43] Mr. Porter agreed to check the Body Shop's records on his return to the United States and to report to Mr. Hedrich. Soon, Mr. Porter called with the Body Shop record of sales at the Halifax Shopping Centre. The amounts needed adjusting to remove sales tax and to match periods, but it appeared that the Body Shop figures for sales were, indeed, substantially higher than those reported to the landlord.

[44] Mr. Porter wrote to Ms. Carson in early October, 2007:

I met with the Landlord while attending a trade convention in Toronto a week ago and they were very reluctant to negotiate. We discussed some ideas and we spoke about sales. Apparently we had a discrepancy with each other's sales numbers and they were due to let me know what period of time they were reporting so we could both talk about the same set of figures. Once they let me know, then we can hopefully get the proposal resolved, but please know there was little to no give in their counter. I will let you know more once they advise of the sales issue and counter back my offer.

[45] A month later, the situation appeared grim:

Year	BS Sales Records	Gross Revenue Reported	Discrepancy
2004	\$1,048,681	\$419,405	\$629,276
2005	1,170,070	392,299	777,771
2006	1,229,412	450,480	778,932.

Sales tax and other credits had to be backed out of sales to arrive at gross revenue, but that could not explain the size of the discrepancy.

[46] Mr. Porter wrote to Ms. Carson on Tuesday, November 6, 2007:

As you're aware we are in the midst of negotiating with the Landlord for Halifax Shopping Centre; however, we are at an impasse regarding a grave discrepancy between what the Landlord currently has on record for your sales and what we are capturing via our internal POS reporting. I've attached a spreadsheet comparing these two recordings and would like some open discussion about an explanation for this significant difference. Feel free to either call me directly or put together an email explaining the reason for the variance between these two series of numbers.

The Landlord is wanting to resolve this matter prior to moving forward with finalizing our renewal negotiations, so you can appreciate the need to move expeditiously with the ultimate resolution of this matter.

At first, Ms. Carson responded in a tone of urgency and cooperation: "Will look into this right away and get back to you ... hope to have more for you by Monday."

However, by the next day, Wednesday, November 7, she scolded: "Has the opportunity to [negotiate] with the landlord been side railed by not coming to me first to sort this out, before bringing them into the discussion?"

[47] Even in her submissions at trial, Ms. Carson was highly critical of Body Shop for informing the landlord of the discrepancy in sales figure. The General Counsel for Body Shop, Mr. Iain Rubli, testified that Body Shop did not agree with the implication that it had to defer to Ms. Carson after the landlord brought up the problem, that it had to seek her explanation and otherwise remain silent.

[48] Mr. Porter replied, "Regardless how we arrived at the discussion with the Landlord, it was one needing immediate resolution." In reply, Ms. Carson described numerous problems her business was handling, including:

My office manager is new. It's Christmas at The Body Shop we are very busy.
My old office manager is no longer with the company nor in the country.

She said, "Am attempting to get you the info as best as possible ...", but she remained focussed on "I completely disagree with you on ... the discussion with the Landlord doesn't have bearing." "Has this situation been brought before the

landlord before you got clarification from me?" (Six years later, we have no clarification from Ms. Carson.)

[49] The next day, Friday, November 16, 2007, Deborah Jackson of Body Shop Canada offered to help with the request for a "Sales Comparison". She asked for a meeting. Ms. Carson rebuffed her in a way that shows Ms. Carson was not as interested in providing "clarification" as she was in debating the propriety of The Body Shop communicating with one of The Body Shop's landlords: "I'm not requesting information from you Deb. I'm requesting it from Mike with respect to relationship with the Landlord. What exactly did [you] want to discuss?"

[50] Months had passed since the discerning Mr. Hedrich had detected there was something wrong with the sales figures reported by the Halifax Sopping Centre Body Shop. 20Vic was not prepared to resume negotiations for a new lease, until outstanding rent was paid. The lease would terminate at the end of the next March. Despite the initial rebuke, Ms. Carson permitted Ms. Jackson to work on a sales comparison, and Ms. Carson produced her own statement.

[51] Early in January of 2008, Ms. Carson produced a list of dates and numbers for "the sales for Halifax Shopping Centre". Although she claimed, "The information comes from our accounting records and are reconciled against bank statements", the numbers match neither. Body Shop rightly rejected Ms. Carson's unjustified figures.

[52] As I said, Ms. Jackson was permitted to work on the sales comparison. On February 20, 2008, Mr. Porter provided a reconciliation to Mr. Hedrich. The conclusion was that Body Shop Canada had underpaid OPB \$49,272 in percentage rent at the Halifax Shopping Centre for the period of August 2004 to July 2007. Body Shop Canada tendered that amount. In response, OPB exercised its right to conduct an audit of the gross revenues for the entire term.

Fraser Howatt Audit

[53] The audit was conducted by Fraser Howatt in March and April, 2008. Mr. Tony Howatt, CA, did the planning, supervised the field work, and provided the opinion. Ms. Cindy Marshall, staff accountant, did most of the field work. Both testified.

[54] Fraser Howatt reviewed the sales summaries submitted monthly by Dawn Carson Enterprises to its chartered accountants during the two-year period from April 2006 to March 2008 and found no errors. As the problem with the reports of gross revenue in those two years did not result from errors in capturing or recording sales in the company's accounting system, Fraser Howatt recommended accepting the company's statements of sales for the rest of the term of years without audit. This would save time and money. 20Vic agreed.

[55] Fraser and Howatt completed the audit and signed an opinion on April 17, 2008. The first year was rent-free. Every month of every year after that Dawn Carson Enterprises reported gross revenue to 20Vic that was less than its own records showed. The annual under-reporting ranged between a hundred and four hundred thousand dollars:

1999	103,436.83
2000	163,276.87
2001	249,863.84
2002	268,318.26
2003	324,152.75

2004	349,051.37
2005	352,338.44
2006	407,928.27
2007	249,667.51.

In a company whose sales, exclusive of taxes collected and held for remittance, ranged between \$840m and \$1.2m, these discrepancies are huge.

[56] Dawn Carson Enterprises had avoided paying nearly two hundred thousand dollars in percentage rent (the \$49,272 tendered by Body Shop Canada in February plus the audit balance of \$148,082). It had paid only about twenty percent of what was owed.

[57] Fraser Howatt calculated interest at prime plus two percent. In its opinion, HST on the outstanding rent would be \$21,821.32 and interest would be \$50,624.99. Adding in the audit invoice of \$12,430, the debt totals \$232,958.37, less the \$49,272.01 tendered by Body Shop Canada in February.

Why Gross Revenue Went Under-reported

[58] Ms. Carson testified that, when 20Vic raised questions about reported gross revenue and Body Shop indicated their computer records showed higher numbers, she felt her numbers were right. By that she meant that the figures she reported were right.

[59] She complained that Body Shop was constantly asking for "my figures". She testified that she did not have copies of all the gross revenue reports she delivered to the landlord. She only kept a copy of the sheet from the previous year.

[60] She says that there were four sets of figures by the time of the audit: her reported or reconstructed figures, the Body Shop original figures, figures produced by the franchise association, and the Body Shop comparative figures. She remained "strongly of the view that our figures were right".

[61] When the audit was underway, Mr. Howatt explained to Ms. Carson "what exactly happened". The accountants discovered "we were double backing out all

things deductible". She broke down. "All along we had meticulous records. How could this error happen?"

[62] Mr. Howatt does not confirm such a conversation. When he recommended stopping the audit of the sales, he said that, so far, the audit revealed that the problem did not result from the record of sales; it resulted from Ms. Carson "starting with accurate sales amounts and the making adjustments for gift card sales, etc., that was not correct." However, as Mr. Howatt pointed out during cross-examination, he was not retained to determine how the problem arose, he was retained to audit gross revenues.

[63] As I said, doubling deductions when calculating gross revenue could not explain the huge discrepancies.

[64] Ms. Carson also advances various theories to suggest that the auditor's figures may not be accurate. The calculation of gross revenue does not allow for two for one sales, giveaways, samples, or inventory taken for use off site. As Mr. Howatt explained, gross revenue is about cash. These things are accounted through inventory and do not affect gross revenue.

[65] Ms. Barbara Foote, the staff person who was in charge of books and accounts at Dawn Carson Enterprises, gave evidence about the under-reporting of gross revenue. She was called by Body Shop Canada.

[66] Ms. Foote was as careful about her testimony as she was careful with financial recording for Dawn Carson Enterprises. She is now an employee of Body Shop, but she had, and retains, respect for Ms. Carson.

[67] I found Ms. Foote to be a straightforward witness. Her evidence is reliable, and I rely on it. Ms. Foote was hired to work at the Bayers Road shop in 1994. She moved to the Parklane shop, then to the Halifax Shopping Centre shop when Ms. Carson moved there in 1998. A year later she became Dawn Carson Enterprises' office manager for both shops.

[68] The position of office manager covered both shops. Out of an office behind the Halifax Shopping Centre shop, Ms. Foote, in conjunction with Ms. Carson, was responsible for the administration of Dawn Carson Enterprises. She looked

after the bookkeeping and other financial recording of both shops. She prepared the monthly package for the accountants.

[69] In her direct examination, Ms. Foote led us through source documents, reconciliations, adjustments, and recording on an Excel spreadsheet. The spreadsheet showed daily sales and adjustments to net out gift certificate sales and redemptions, HST, refunds, and exchanges. Thus, the net sales netted out more than that expressly provided in the Halifax Shopping Centre lease for calculating gross revenue.

[70] The Excel spreadsheet also recorded amounts for "tester", "staff", till variance, and redemption of gift certificates sold outside the Halifax Shopping Centre and Parklane, but none of these affected net sales.

[71] Each month, Ms. Foote gave the Excel spreadsheet to Ms. Carson. She sent it with the rest of the accountant's package to the auditors for Dawn Carson Enterprises. She did not, however, send it to 20Vic or OPB.

[72] Ms. Carson instructed Ms. Foote to deliver the net sales figures to Ms. Carson and let her report to the landlords. Once or twice a year, Ms. Carson asked whether the numbers had "the subtractions" taken off, and she was assured that they had been.

[73] When a representative of a landlord called about the gross revenue number, Ms. Foote took down the number and relayed the inquiry to Ms. Carson. That is what Ms. Carson had asked her to do.

[74] In cross-examination, Ms. Foote was asked about numerous computer problems Dawn Carson Enterprises experienced with Body Shop systems, especially after the involvement of L'Oréal. The system sometimes crashed. Staff had to do manual receipts. The software system for debit and credit cards caused numerous problems.

[75] "Head office", either Toronto or Raleigh, had access to the franchisee's computer. Misuse caused inventory files to disappear. There were problems with errors on head office invoices. Ms. Foote found herself spending too much time correcting head office records.

[76] L'Oréal imposed promotions. Unsolicited product arrived and disposition was the franchisee's problem.

[77] The problems multiplied during the busy season of November and December. The debit and credit card system crashed often. The system induced errors in sales that required manual correction. Sometimes that required daily inventories. Numerous errors were made in product orders, and that also required staff time.

[78] In re-examination, Ms. Foote was asked whether inventory and software problems affected the calculation of net sales. She said that they did not. She also agreed that the failures of the debit and credit card software did not prevent her from coming to what she considered to be the correct sales figures.

[79] I find that each month of each year, Ms. Carson was given accurate net sales results for the Halifax Shopping Centre shop. I find that each month of each year, Ms. Carson reported to 20Vic and OPB gross revenues that were drastically less

than actual net sales. I find that the under-reporting resulted from Ms. Carson choosing to drastically reduce accurate numbers.

The Understatement and Ms. Carson's Good Character

[80] The defence goes so far as to submit that if I find Ms. Carson is a "fraudster", her claims and defences fail. The submission to the contrary is that I should find that Ms. Carson is the kind of person who could not deliberately mislead so as to avoid rent.

[81] To this end, the defence asked Ms. Carson's neighbour and "fellow entrepreneur", Margaret Armour, about Ms. Carson's reputation in the community. An objection was registered, and I agreed to hear the evidence and rule on admissibility later.

[82] Ms. Armour said that Ms. Carson was known to be "good, kind, fair". That was her reputation in the neighbourhood. In business, "Her approach was inspiring." She would never be dishonest. It is impossible to believe she stole money.

[83] Ms. Armour's testimony is a good example of the difficulties faced by a party who travels down the good character road. The subject is limited to evidence of general reputation: see the discussion at para. 13 of *R. v. Beland*, [1987] 2 S.C.R. 398.

[84] A serious witness, such as Ms. Armour, finds herself confronted with a fuzzy subject, general reputation, and heads for the concrete. First, what do the neighbours think of her? Then, her approach to business, not her reputation at all. Finally, the real subject. She is not dishonest. She is not the kind of person who would mislead a landlord to avoid rent.

[85] Except possibly the testimony about the neighbourhood, all of this offends the limit, general reputation. It takes us into inadmissible territory about kinds of people. Assuming an implied foundation, the testimony about what the neighbours think is a small sampling for general reputation.

[86] We heard other testimony about Ms. Carson that seemed to be ordered towards a finding about different kinds of people. Ms. Foote, for example, was

asked in cross what Ms. Carson was like to work for, and she gave a favourable report.

[87] I am not called upon to decide whether Ms. Carson admitted a fraud, let alone whether she deserves the characterization "fraudster". However, I am called upon to determine what Ms. Carson did with those monthly gross revenue reports. She may have been conscientious about other aspects of her business, she may have been a pleasure to work for, she may have kept and remitted every cent of sales tax, she may have paid all her rent at Parklane, she may have been of service to others in the community. None of that changes the hard facts of this case:

- Ms. Carson did not let her office manager, who provided meticulous accounting reports, prepare the gross revenue reports.
- Unlike every other financial document of Dawn Carson Enterprises, the gross revenue reports were destroyed annually.
- Ms. Carson had accurate net sales figures at hand when she prepared the reports.

- She was told repeatedly that the gross revenue subtractions had been made in the net sales figures.
- She filled in gross revenue reports that understated the revenues drastically.
- There is no evidence of a method, only drastic unexplained reductions.
- The misrepresentations were repeated monthly, every year for almost a decade.
- As a result, Ms. Carson's company paid only a fifth of the percentage rent due for the Halifax Shopping Centre shop.

[88] I find Ms. Carson drastically understated her company's Halifax Shopping Centre gross revenues in her reports to the landlord and avoided paying rent that was due.

Consequences of the Default

[89] Clause 6.1.25 of the subfranchise agreement gave Body Shop Canada rights to audit the businesses at both locations. It provided "the Sub-Franchisee shall bear the costs incurred by the Franchisee in verifying the Sub-Franchisee's accounts ...".

[90] Body Shop Canada had its own audit done. It did so for two reasons. Firstly, it did not know whether it could rely on the Fraser Howatt audit. It was not the client. Secondly, it was concerned about Parklane, where Body Shop Canada was the tenant and Dawn Carson Enterprises had been responsible to report gross revenues and pay percentage rent.

[91] PricewaterhouseCoopers was retained. It reported in May, 2008. Its conclusions for Halifax Shopping Centre were close to those of Fraser Howatt and it did not find large under-reporting at Parklane. The work cost \$25,473.

[92] As I said, discovery of the default led Body Shop Canada to make an initial payment of \$49,272 to 20Vic, which was intended to cover three years rent arrears. 20Vic, in turn, exercised the audit powers under the lease. OPB sued Body Shop Canada and Dawn Carson Enterprises. Body Shop Canada settled for \$156,132 in December, 2008.

[93] As part of the settlement, OPB agreed to allow overholding until a new lease was signed. OPB would have seven months to complete the renovations; a deadline of June 30, 2009. Terms for the new lease included: "Tenant: The Body Shop Canada Limited".

[94] At about the same time as the settlement in December of 2008, Body Shop Canada made demand on Dawn Carson Enterprises. It had repaid \$34,476 of the \$49,272 and the demand was for \$171,028. Payment was required by January 12, 2009 or Body Shop Canada would terminate the sublease and take possession of the Halifax Shopping Centre shop. In reliance on cross-default provisions, Body Shop Canada would also terminate the Parklane sublease and take possession.

[95] Dawn Carson Enterprises argues that the amounts demanded were excessive because sections 3.7 and 3.8 of the lease limit liability for arrears of percentage rent. See para. 26 to 32 of this decision for the textual context and para. 33 and 34 for the text of s. 3.7 and s. 3.8.

[96] Section 3.7 requires the tenant to create, control, and retain proper sales records. It does not limit liability. Further, the retention period is "not less than" eighteen months. The phrase "not less than" is inconsistent with a limit on liability. Indeed, the liability to pay percentage rent is in s. 3.2:

Tenant shall pay to Landlord ... further rent equal to the amount, if any, by which ... [6%] of Gross Revenue ... exceeds Basic Rent

This liability is not limited.

[97] If the tenant destroys sales records that are older than the eighteen month minimum period, the landlord would still be free to try to prove under-reporting of gross revenues and underpayment of percentage rent through other sources. In this case, that was not necessary because proper sales records were created, controlled, and retained throughout the term.

[98] Dawn Carson Enterprises argued that the audit rights expire after a reasonable time. Body Shop Canada referred me to *Danforth-Woodbine Theatre Ltd. v. Loblaws Inc.*, [1999] O.J. 2059. In that case, inspection rights "upon reasonable notice" were interpreted as applying to past statements, as opposed to the current statement. Justice Juriansz interpreted the lease as providing "a right to inspect the tenant's books and records for any year for which there may be a legal liability for outstanding rent arrears": para. 73.

[99] Our situation differs from *Danforth-Woodbine Theatre*. The audit rights under s. 8 are not exercisable "on reasonable notice". The rights are limited to a reasonable time. It is arguable that eight years is not reasonable, if it is arbitrary.

[100] However, the audit rights under s. 3.8 do not give the tenant a pass. The right applies, "At any reasonable time after delivery or failure to deliver to Landlord any statement referred to in section 3.6.1 ...". Soon after the tenant advises there was significant under-reporting for three years would be a reasonable time for an audit of the whole term.

[101] Further, neither the tenant nor the subtenant objected to the audit. At a minimum, it yielded solid evidence of rent arrears and nothing in the lease precludes use of that evidence.

[102] I find support for this view in *Michigan Avenue National Bank v. Evans, Inc.* (1988), 176 Ill. App. 3^d 1047, to which Body Shop Canada referred. The lease in that case provided for audit rights for two years after delivery of statements and it required records retention for three years. The Illinois Appellate Court held that those periods did not limit liability to anything shorter than the period in the applicable statute of limitations: p. 1059 - p. 1060. Our statute limits actions for rent to twenty years after the cause arose: *Limitation of Actions Act*, s. 2(c).

[103] The consequences of the proven default follow logically under the terms of the lease. The default justified termination of the sublease and taking possession under the head lease.

Ms. Carson's Complaints

[104] Over the years, the Body Shop business became less and less attractive for the subfranchisees. Many gave up. Few remain.

[105] Ms. Carson seeks a finding that L'Oréal, with the assistance of Body Shop Canada, 20Vic, and OPB Realty, "knocked off one more of the 'independents' " and "reaped the benefit of all of the good will that Ms. Carson had developed".

[106] In support of her allegations of "Breach of Contract, Breach of Fiduciary Duty, Equitable Fraud, Tortious Interference, Breach of Implied Duty of Good Faith and Fair Dealing, Economic Duress, Extortion, etc.", Ms. Carson presented evidence about head office computer and accounting failures, delivery of unwanted product, the conduct of negotiations after the default comes to light, refusal of ADR, breach of supposed confidentiality, and breach of exclusivity.

[107] On the computer and accounting problems, see para. 74 to 77 above. I find that there were extraordinary problems with point of sale computer recording, operation of the computer system, and head office accounts.

[108] However, I do not find these problems were deliberately caused, were restricted to subfranchisees, or went unresolved. They were resolved at the expense of much staff time. I find that these problems had nothing to do with under-reporting gross sales at one location, the Halifax Shopping Centre.

[109] Ms. Carson also attempted to show that negotiations to settle the claim for percentage rent and for renewal of the leases were carried out in bad faith. The opposite is true.

[110] After discovering the drastic under-reporting of gross revenue by Dawn Carson Enterprises, 20Vic decided it would not consent to a Carson subtenancy under a new lease. I find that position was reasonable in the circumstances.

[111] Body Shop Canada convinced 20Vic to change its mind. If Dawn Carson Enterprises met Body Shop's standards, 20Vic would accept it as subtenant.

[112] There were negotiations, at first for continued operations, then for buyout. Body Shop Canada acted reasonably throughout. It decided to end the negotiations because the parties were too far apart.

[113] One alleged sign of bad faith negotiations is the refusal to take up processes suggested by Ms. Carson for determination of the amount owing for percentage rent, such as arbitration or an application. In my view, the parties were free to agree to or decline ADR. Dawn Carson Enterprises was free to start an application.

[114] Another complaint that makes little sense concerns L'Oréal having given information to 20Vic about Dawn Carson Enterprises' sales. See para. 41 to 51 above. Ms. Carson's theory of confidentiality owed to her and agencies at play in lease negotiations ignore that Body Shop Canada owed a duty of good faith to the landlord and was on the hook for the rent her company had failed to pay.

[115] Another complaint is that the landlord did not honour the exclusivity term in the head lease and deprived the subtenant of the advantage of lessened

competition. This goes back years. No action was started by Dawn Carson Enterprises, and no loss was proven.

Conclusion

[116] Ms. Carson's company broke faith with its franchisor and its ultimate landlord by drastically under-reporting gross revenues, and seriously underpaying percentage rent, at the Halifax Shopping Centre Body Shop. The underpayment and under-reporting justified termination of the sublease, refusal to negotiate a new one, termination of the franchise agreement, possession of the two Body Shops, and the suit for the unpaid rent. Therefore, one of those found any cause against Body Shop Canada, OPB Realty, or 20Vic Management.

[117] I will allow the claims by Body Shop Canada against Dawn Carson Enterprises as subtenant and subfranchisee and against Ms. Carson as guarantor. I will grant judgment for \$171,028 plus prejudgment interest after December 12, 2008.

[118] I will dismiss the counterclaim and the third party proceeding. I reserved on a motion for non-suit on the third party proceeding. I chose to leave the motion in its academic state because the testimony of Mr. Hedrich and Mr. Blaise Morrison assisted the fact-finding in reference to all of the defendants' defences and claims.

[119] Parties may make submissions on costs in writing.

Moir J.