

## CORPORATE FINANCE BULLETIN

June 2004

### THE NEW LIMITATIONS ACT - ITS IMPACT UPON DEMAND OBLIGATIONS

The new Ontario *Limitations Act, 2002* (the "Act"), which came into effect in January 2004, reduces the limitation period for actions from six years to two years, subject only to specific exceptions. Consequently, a lawsuit must now be brought within two years from the date that the underlying "claim" was discovered or should have been discovered. Otherwise, the ability to pursue an action with respect to a claim will be statute barred if the claim is not made within the two year limitation period. A "claim" is defined under the new Act as "a claim to remedy an injury, loss or damage".

#### DEMAND LOANS

##### *Two Year Basic Limitation Period*

The reduction in the limitation period from six years to two years is of particular note with respect to demand loans. Courts have previously established that promissory notes that are payable on demand create an obligation to pay from the time that the promissory notes were entered into. Accordingly, the limitation period with respect to demand loans has historically been calculated from the time that the promissory note was created. However, given the language of the new Act, one could argue that a "claim" (as defined by the new Act) would arise only upon demand under the note being made, since only then would loss or damage under the promissory note be established. As such, the limitation period would now be calculated from the date of demand and not from the date that the promissory note was entered into, as was previously the case. Nevertheless, until this issue is determined by a court, the more prudent approach would be to assume that the new two year limitation period continues to be calculated from the date that the demand promissory note was entered into.

##### *Restarting the Clock*

The new Act does provide some relief from the reduced limitation period. The Act effectively acknowledges the ability to renew the two year limitation period by "restarting the clock" for its calculation upon the obligor's acknowledgement of the claim. The acknowledgement can take of the form of partial payment of the indebtedness, including payment of interest, or written acknowledgement of the indebtedness. Any such acknowledgement will restart the two year clock as at the date of such acknowledgement subject, however, to an "ultimate" limitation period of fifteen years stipulated by the new Act.

##### *Fifteen Year Ultimate Limitation Period*

The ultimate fifteen year limitation period begins to run from the *date that the underlying act or omission giving rise to the claim took place*, regardless of when the claim was discovered or should have been discovered. In the case of a demand loan, the fifteen year ultimate limitation period is calculated from the date of default under the demand obligation.

#### NO CONTRACTING OUT

Prior to the new Act, parties were free to shorten or lengthen by agreement the applicable limitation period. The new Act, however, provides that the limitation period "applies despite any agreement to vary or exclude it". Consequently, under Ontario law, parties can no longer establish a limitation period other than that which is prescribed or provided for under the new Act.

One possible option that lenders not wanting to be restricted by the terms of the new Act could explore is to opt for their agreements to be governed by the laws of a jurisdiction other than Ontario and where such laws do not preclude the ability of parties to contract out of statutory limitation periods. However, this option is somewhat limited in scope since the loan transaction must have a legitimate connection with the other jurisdiction chosen such that the governing law selected is not artificial or motivated solely by the desire to avoid application of the new Act.

## RECOMMENDATIONS

In summary, given the new Act, lenders are well advised to be diligent in monitoring their demand loans and any default thereunder, including:

- diarizing the dates for expiry of limitation periods. As noted, until otherwise determined by a court, we recommend calculating the limitation period from the date that the demand note was entered into;
- obtaining written acknowledgements of the indebtedness prior to expiry of the applicable limitation period, to the extent that interim payments in respect of the indebtedness are not being made prior to such expiry. In the case of such written acknowledgements, we recommend that all debtors and guarantors sign such acknowledgements; and
- incorporating into forbearance or similar agreements, an acknowledgement of the indebtedness, to the extent that a separate written acknowledgement is not then also being obtained.

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*The foregoing provides only an overview. Readers are cautioned against making any decisions based on this material alone. Rather, a qualified lawyer should be consulted.*

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