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The Limitations Act and Debt Claims

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Under Ontario's new Limitations Act 2002 (the "Limitations Act" or the "Act") it is essential that businesses consider the potential expiry of limitation periods on an ongoing basis. Claims discovered after December 31, 2003 generally now expire after two years, rather than after six years as was the case under the predecessor legislation. This shorter two year period applies to most claims including those based upon breaches of contract and torts discovered after December 31, 2003.

Recent amendments to the Act have introduced greater flexibility for commercial parties. As originally enacted, the Act prohibited all attempts to contract out of the limitation periods prescribed by the Act. In response to widespread criticism, the Act has been amended to afford parties in a business relationship greater freedom to establish their own time limitations for commencing legal proceedings to assert a claim.

The Ontario Limitations Act, 2002

The Limitations Act came into effect on January 1, 2004, replacing the prior legislation, which was widely believed to be excessively convoluted with several

categories of claims. The limitation periods under the Limitations Act, which apply to all claims that arise after December 31, 2003, are as follows:

- i. the basic limitation period is now two years (previously six years) from the date that a person discovers or ought to have discovered the circumstances entitling him or her to make a claim;
- ii. an ultimate limitation period of fifteen years runs from the date that the act or omission on which the claim is based took place; and
- iii. no limitation period for certain claims, including undiscovered environmental claims.

There are some exceptions to the general rules, including where the potential claimant is a minor or mentally incapacitated, where the Act specifically confirms a different limitation period in another statute, or where the existence of the claim is willfully concealed. Also, claims involving real property are addressed under the Real Property Limitations Act (Ontario). Most other claims, including simple debt claims, will

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fall under the basic two-year limitation period.

Commencing the Clock on the Limitation Period

A “claim” for the purposes of the Limitations Act is defined at section 1 as being “a claim to remedy an injury, loss or damage that occurred as a result of an act or omission.” For demand loans, as well as bills of exchange and promissory notes payable on demand, it is not entirely clear when the “act or omission” has occurred or when the “injury, loss or damage” is suffered. The previous common law position was that the debtor’s obligation to pay a demand obligation arose as soon as the obligation was incurred, and that demand was not necessary. Accordingly, the cause of action arose—and, therefore, the limitation period commenced—as soon as the demand obligation was incurred. It is hoped that, given the short two-year limitation period under the new Act courts will interpret the limitation period as running from the date of an unsatisfied demand. This approach is clearly more consistent with commercial reality. However, to date, the question has not been considered by any court and there is a risk that a demand obligation created after December 31, 2003 will not be enforceable more than two years after the date of its creation.

For term loans, neither the occurrence or the discovery of a misrepresentation, breach of covenant or other default or event of default under a credit agreement or security document nor the making of demand to accelerate payment will of itself constitute an “injury, loss or damage” necessary to start the limitation period. Rather, it is the failure to pay when lawfully required to do so that causes injury or loss to the creditor that starts the limitation period’s clock.

Acknowledgement of Liability

Pursuant to section 13(1) of the Limitations Act, an acknowledgement of liability in respect of a liquidated sum restarts the limitation period for that debt. Likewise, an acknowledgement in respect of interest will restart the limitation period in respect of the principal, as well as future interest pursuant to subsection 13(2). However, one should note that the acknowledgement must be made to the creditor (or his agent or trustee in bankruptcy) before the expiry of the applicable limitation period pursuant to subsection 13(9).

The predecessor legislation did not specify the form of the acknowledgement required. Under subsections 13(10) and 13(11) of the Limitations Act, acknowledgement can take the form of a partial payment of principal or interest or a written acknowledgement of the indebtedness, signed by the debtor or his agent. Accordingly, the prudent approach is to obtain a written acknowledgement of an amount owed, specifying that it relates to both principal and interest where no payment has been made, particularly in circumstances where an extension of time is being provided for payment of the debt.

Agreements to Vary the Limitation Period

At common law, it had generally been possible for parties to agree to lengthen, shorten or not enforce a limitation period. When the Limitations Act was enacted, however, section 22 of the Act removed this freedom, providing that the Act’s limitation provisions applied regardless of any agreement to exclude or vary them. This raised the concern that provisions in commercial agreements, such as asset purchase and sale agreements, that attempt to limit the assertion of a claim to less than two years from the occurrence of a breach, may not be enforceable. Similarly, it appeared that parties would no longer have the freedom to enter into “tolling agreements”

whereby, despite the existence of an enforceable claim, the claimant would agree with the potential defendant not to commence proceedings without prejudice to the claimant's right to do so at a later point in time despite the expiry of the applicable limitation period. Such agreements to "suspend" the running of the limitation period were often valuable in affording the parties an opportunity to reach a negotiated solution to their dispute or to allow the claim to crystallize.

Bill 14, entitled the Access to Justice Act, 2005, which came into force on October 19, 2006, amended section 22 of the Limitations Act. While the general prohibition on contracting out is retained, significant exceptions now allow any claimant to enter into an agreement with a potential defendant to suspend or extend a limitation period prescribed by the Act, thereby restoring the freedom to enter into tolling agreements. Furthermore, parties to "Business Agreements", defined as agreements made by parties none of whom is a consumer as defined by the Consumer Protection Act, 2002, may enter into agreements varying or excluding the Act's limitation periods. Therefore, parties to commercial contracts—but not consumer contracts—are free to stipulate limitation periods other than those prescribed in the Act.

It should be noted, however, that the amendments apply only to agreements made on or after October 19, 2006. Therefore, any agreement made between January 1, 2004 and October 18, 2006 that purports to vary or exclude the Act's provisions would be ineffective.

Successors, Principals, and Agents

Successors to a claim shall be deemed to have knowledge of the claim on the earlier of: (i) the day the predecessor first knew or ought to have known of the claim, or (ii) the day the successor first knew or ought to have known of the claim, at which point the two-year limitation period will begin to run.

Likewise, in the case of a proceeding commenced by a principal, if the agent had a duty to communicate knowledge of a claim to the principal, the principal shall be deemed to have knowledge of the claim on the earlier of the day the agent first knew or ought to have known of the claim.

In determining what is the day the predecessor or agent first ought to have known, subsection 12(3) provides that it is the day on which a reasonable person in the predecessor's or agent's circumstances and with the predecessor's or agent's abilities first ought to have known of the claim.

Conclusion

The new Limitations Act brought about several changes to enforcement of claims in Ontario, including a much shorter limitation period and changes in the process of acknowledging claims. In order to protect against avoidable loss from the inability to pursue a claim under the new rules, it is advisable to acquaint oneself with the new procedures under the Limitations Act if one has not already done so. Fortunately, the new amendments introduced by the Access to Justice Act, 2006 increase the ability of parties to adapt the limitations rules to their individual needs.

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