

April 2007

DEMAND NOTE

You may place Hare v. Hare [2006] O.J. No. 4955 (C.A.) in the Reuben Rosenblatt category of "cases that scare me."

The Note

Mother loaned \$150,000 to son in 1997; she took back a demand interest-bearing note to evidence the loan. Son stopped making interest payments in October 1998. Mother demanded payment on the loan in November 2004, but received no payment. In January 2005, she commenced an action against son. Son defended, relying upon the Limitations Act and the Limitations Act, 2002.

Common Law

You may have thought that the cause of action under a demand note did not arise until demand was made. You would have been wrong. A cause of action "is simply a factual situation the existence of which entitles one person to obtain from the court a remedy against another person." Accordingly, under common law, since a "demand loan is fully mature and repayable when it is made, a cause of action to collect on a demand note accrues as soon as the note is delivered."

Accordingly, under the old Limitations Act, a cause of action died six years after a note was delivered, unless the limitations commencement date was extended to a later date, such as the date on which the debtor made any payment, interest or principal, on the note or the

debtor acknowledged in writing the existence of the debt.

In the Hare circumstances, under the old Act the cause of action would have died after October 2004. The question was: which of the Acts applied, old or new?

Limitations Act, 2002

The new Act, proclaimed on January 1, 2004, has a basic two-year limitation period. Subject to transitional rules, that period runs from the date a claim is or ought reasonably to have been discovered. Section 5 of the new Act states that a claim is discovered on the earlier of the date a person first knew that (i) the damage had been incurred and (ii) an action would be appropriate to seek a remedy.

The majority of the Court interpreted section 5 to mean that, for a demand promissory note, the claim is discovered on the date that the note is given. The majority gave three reasons:

1. The language of the new Act is different from the language of the old Act, but it is not "so irresistibly clear that the court could presume that the legislature intended to depart from established commercial law and disturb existing common law rights."

2. If a demand triggered the start of the period and there was no demand, then the limitation period would never run and liability would exist indefinitely. This, the majority stated, was not good.

3. The discoverability principle under the old Act was created by common law to

ensure that a limitation period would never run its course before a claimant even knew there was a cause of action. There was no such problem with a demand note because a lender does not need to discover anything to become aware of the claim.

The minority disagreed. He felt that:

1. The language of the new Act is sufficiently different; it refers to knowledge that a proceeding would "be an appropriate means to remedy" the damage. The common law talked instead about when a lender would be "entitled to bring a proceeding." The lender under a demand note might be **entitled** to bring a proceeding, but until the lender demanded payment, it would not be **appropriate** to do so. Further, section 5 talks about "having regard to the nature of the damage." The damage is latent until the lender makes demand and the nature of the loss only becomes apparent when the lender realises that that the damage is actual, not latent. Finally, although a person is entitled to commence an action without demand (because the action is the demand), a reasonable person would not actually do so without making demand. Why commence an action unnecessarily? That would hardly be an **appropriate** means to remedy the damage.

2. What is so bad about a limitation period that never starts running? Under section 15(6) of the new Act, which deals with the 15-year limitation period, the act or omission starting the period is "in the case of default on performing a demand obligation, the day on which the default occurs." Accordingly, the new Act recognises that a demand loan could run until demand is made.

Transition

The majority applied the transitional rules to determine that the lender had discovered the cause of action before January 1, 2004 and that the limitation period under the old Act applied. Accordingly, the claim died six years after October 1998. The minority stated that the claim was not discovered before January 1, 2004; therefore, the new Act applied, the period started when demand was made, and the action was commenced in time.

For what it is worth, we find the minority's reasons much more compelling.

Postpone Demand

What if the promissory note is stated to be payable 10 days, or even five years, after demand? We would argue that the points that the majority makes about a lender being able to commence an action immediately, such that the limitation period runs immediately, are inapplicable. If the lender commences the action before demand, the lender is not able to say, "you owe me the money now." Accordingly, the lender is not able to commence the action immediately and the cause of action has not arisen.

More Paper

In our last newsletter, we discussed the case of Liorti v. Menzies [2005] O.J. No. 5564. In that case, you may recall, mother's mortgage was secondary collateral to son's primary mortgage and the lawyers dealt only with son. We reported that the essence of the decision of the trial judge was, "*son and mother were clients and since mother was liable for the full loan, the lawyers owed a duty to obtain her instructions; they did not do*

so and, accordingly, the payment of the proceeds was a breach of trust."

Unfortunately, by the time that we reported on the decision, it had, unbeknownst to us, been reversed on appeal in December 2006. We had not noted up the case because, normally, all of the cases upon which we report are so recent that they are the last word. So here is a word of advice that we did not follow: always update your cases.

Reversal

The Court of Appeal reversed the trial judge at [2006] O.J. No. 4872. The trial judge had decided that mother's mortgage was secondary and not primary, but held that this determination was unimportant; the real question was whether the lawyers held the mortgage advance in trust for both son and mother. The Court of Appeal held that the

decision that the mortgage was secondary security answered the real question. The consideration that mother received for her mortgage was the advance of the money on the primary mortgage to son; therefore, the lawyers held the monies in trust for son and not for her.

Hindsight

We made some hindsight comments in our previous analysis. The result in the case may have changed, but our comments about practising defensively do not. Had the lawyers acted for the mortgagee only, the lawyers would have obtained a direction for funds from mother and son and the action would not have arisen. Had the lawyers acted for only mother and son, the action would not have arisen. Had the lawyers acted, as they did, for both parties, but obtained a direction, as they would have done had they acted only for the mortgagee, there would have been no action.

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