



Demand Shareholder Loans – Make Sure They Don't Become Statute Barred

The Issue:

When does a demand loan become statute-barred? How is this relevant to, among other things, your client's creditor-proofing and corporate/estate planning structures?

The recent Ontario Court of Appeal decision in *Hare v. Hare* confirms that the 2-year limitation period in Ontario's new *Limitations Act, 2003* applies to demand loans from the date the loan is made and not from the date of demand. Each time a payment or acknowledgement of the debt is made, the 2-year clock gets restarted. To the business community, this result is not intuitive at all since it would make more sense if the 2-year clock started from the time demand was actually made. This, however, is not the law.

Why You Should Care:

As accountants and lawyers, we are involved in documenting the creation of demand shareholder loans. Often (but not always) promissory notes are created, secured and then forgotten about. No payments or acknowledgments are ever made. This is particularly true with demand notes that are issued as part of a creditor-protection, estate or tax planning reorganization. In an insolvency situation, if no payments or acknowledgments have been made under these demand loans for the past 2-years, it would be open to a receiver or trustee to challenge the enforceability of the corporate obligation on the basis that it became statute barred. In such case, the security would not support any underlying debt obligation and the client suffer a loss of the entire loan.

In addition to the commercial implications, a statute-barred debt can have serious negative tax implications for the debtor corporation under CRA's debt forgiveness rules.

What You Can Do About It:

There are at least three (3) practical means to avoid this unintended result: (a) create a process for annually "acknowledging" the debt (perhaps as part of the "annual resolutions"), (b) ensure some payment is made at least annual on the debt and (c) ensure the debt is evidenced by a proper promissory note which extends the 2-year limitation period to a suitably longer period.