Goodmans LLP Update

Arbitration Preconditions can Suspend Commencement of a Limitation Period

In *PQ Licensing S.A. v. LPQ Central Canada Inc.*, the Ontario Court of Appeal recently upheld an arbitrator's decision that the two-year limitation period commenced on the date the mediation requirement in the parties' contract was deemed to be fulfilled. In the result, the claim was not statute-barred by the *Limitations Act, 2002* (the "**Act**"), despite the claimant initiating arbitration four years after the claim was otherwise discoverable. Parties negotiating commercial agreements that include arbitration preconditions in dispute resolution provisions should be mindful of this decision and consider clarifying their intentions about the staging and timing of steps leading to arbitration.

Background and Decision

Many commercial agreements contain a staged dispute resolution process like the one in *PQ Licensing*. Often these mechanisms call for various levels of negotiation and then mediation as preconditions before a party can resort to arbitration or litigation. These mechanisms are intended to encourage early resolution of a dispute, but it is now clear they may also impact the calculation of a limitation period.

For most claims under Ontario law, including claims commenced by arbitration, the Act prohibits proceedings being brought more than two years after the claim was "discovered". The Act provides for a series of requirements to determine when a claim is "discovered", one of which – section 5(1)(a)(iv) – is the claimant's knowledge "that, having regard to the nature of the injury, loss or damage, a proceeding would be an appropriate means to seek to remedy it". Before *PQ Licensing*, there had been no judicial consideration of section 5(1)(a)(iv) of the Act in the context of a dispute resolution mechanism that provided for mediation as a precondition to arbitration.

In *PQ Licensing*, the parties agreed that absent the requirement for mediation as a first step, the claim (relating to rescission of a franchise agreement) would otherwise have been discovered four years before the arbitration was commenced. The arbitrator determined on the facts before him that the mediation precondition served to suspend the limitation period, as arbitration was not an "appropriate means" to resolve the dispute (as required by section 5(1)(a)(iv) of the Act) until after the mediation condition of the parties' agreement had been fulfilled. Since the mediation condition had been fulfilled less than two years before the arbitration commenced, the arbitrator found the claim was not time-barred. Both the Ontario Superior Court and the Ontario Court of Appeal upheld this decision as reasonable.

Takeaways

While the logic is compelling to avoid the commencement of unnecessary proceedings and allow the parties to focus on an early resolution, claimants should not rely on *PQ Licensing* to delay commencing a proceeding where mediation is a precondition to arbitration without an assessment of "appropriateness" under section 5(1)(a)(iv). Appropriateness will always be based on an interpretation of the particular contract between the parties and assessed on the facts of each case.

However, in light of *PQ Licensing*, it is important for parties negotiating commercial contracts to appreciate the potential implications of including preconditions to arbitration in dispute resolution provisions. Such preconditions could have the effect of postponing the start date of the two-year limitation period beyond the date of when a claimant knows it has incurred a loss. This may, among other things, impact the viability of a limitation period defence.

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