

Plead carefully: SCC clarifies cause of action estoppel and limits on relitigation

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In *Patrick Street Holdings Ltd. v. 11368 NL Inc.*, 2026 SCC 15, the Supreme Court of Canada held that cause of action estoppel barred the appellant from advancing a new theory in a second proceeding to support its entitlement to mortgage proceeds. The Court's decision is an important reminder that litigants must bring forward all reasonably available arguments in the first proceeding, and subsequent attempts to relitigate the same underlying cause of action will likely be barred. Respondents must raise *res judicata* at first instance to rely on its protections, including by properly pleading the underlying material facts.

Background

The dispute arose from a commercial property owned by 11368 NL Inc. and encumbered by multiple mortgages. Patrick Street Holdings Ltd. was one of the secured creditors.

Following a default, Patrick Street exercised its power of sale and prepared an accounting of the sale proceeds. The accounting included a \$4 million collateral mortgage in Patrick Street's favour. In earlier proceedings in 2016, competing encumbrancers challenged the accounting. The court ultimately excluded Patrick Street's \$4 million mortgage from the distribution of the proceeds, which was upheld on appeal.

In 2019, 11368 NL Inc. brought a separate application seeking payment of the remaining proceeds. In response, Patrick Street asserted new arguments supporting its entitlement to the excluded \$4 million mortgage. Both the application judge and the Court of Appeal rejected Patrick Street's position on the basis that the issue had already been determined. The Court of Appeal further found that Patrick Street's claim was barred by the cause of action estoppel.

The Supreme Court of Canada's decision

The test for cause of action estoppel

The Supreme Court of Canada reaffirmed the long-standing test for cause of action estoppel, which has four parts:

1. there must be a final decision of a court of competent jurisdiction;
2. the parties must be the same or in privity;
3. the cause of action must not be separate and distinct; and
4. the arguments advanced in the later proceeding were, or could reasonably have been, advanced earlier through reasonable diligence.

The Court provided new direction on the third and fourth stage of the test, emphasizing that (i) the analysis turns on substance rather than the manner in which claims are framed, and that (ii) courts must focus on the underlying set of material facts giving rise to the claim and assess whether additional legal theories could have been pursued earlier with reasonable diligence.

Applying this framework, the Court held that the 2016 and 2019 proceedings involved the same cause of action and barred Patrick Street from re-litigating its entitlement to the mortgage proceeds, as each proceeding required a determination of the validity, value and priority of encumbrances arising from the sale proceeds. Patrick Street's attempt in the later proceeding to rely on new contractual interpretations and evidentiary arguments was simply a new legal theory grounded in the same material facts.

Limited residual discretion

The Court acknowledged that courts retain a narrow residual discretion to decline to apply cause of action estoppel where doing so would result in an injustice. That discretion is exceptional and typically arises only in cases of procedural unfairness.

No such circumstances were present. The earlier proceeding had fully and fairly adjudicated the accounting, and finality weighed decisively in favour of estoppel.

A functional approach to pleading *res judicata*

The Court confirmed that parties seeking to rely on *res judicata* as a defence must plead or raise it at the earliest opportunity, emphasizing a functional approach to pleading. In particular, the Supreme Court held that:

- the obligation to plead *res judicata* is satisfied where a party pleads the material facts giving rise to the estoppel;
- it is not necessary to expressly use the term "*res judicata*"; and
- the central inquiry is whether the opposing party had fair notice of the case it was required to meet.

On the record before it, the Supreme Court concluded that the respondent had adequately raised the doctrine of *res judicata* through its pleadings and submissions.

Dissenting opinions

Three justices dissented in two separate sets of reasons, each raising distinct concerns about the application of cause of action estoppel in the circumstances.

Justice Côté would have declined to use *res judicata* to bar Patrick Street's claim and would have allowed the appeal. She found that *res judicata* must be raised in the first instance—in this case, before the application judge—and that 11368 NL Inc. had failed to do so. Further, she took a narrower view of the doctrine itself, finding that the later claim was not sufficiently identical in substance to justify foreclosing it through estoppel, as the 2016 proceeding pertained only to the determination of encumbrances of other creditors.

Justice Martin, joined by Justice Karakatsanis, similarly would have found that 11368 NL Inc. failed to raise *res judicata* at first instance, but did not agree that a party should be barred from raising it for the first time on appeal. In their view, the earlier accounting decision did not finally determine Patrick Street's contractual entitlement under the \$4 million collateral mortgage and they would have exercised the Court's residual discretion to permit the claim to proceed on its merits.

Key takeaways

The decision underscores the need for parties to carefully assess, plead, and advance all reasonably available arguments at the earliest opportunity in proceedings involving overlapping factual foundations. In particular, parties should be mindful of the following considerations when structuring and litigating claims arising from the same factual matrix:

- Cause of action estoppel requires parties to advance all reasonably available legal theories arising from the same material facts in the initial proceeding.
- Reframing a claim or advancing a new legal argument based on the same factual foundation will not avoid estoppel.
- The residual discretion to decline estoppel is narrow and exceptional and will not be exercised absent genuine procedural unfairness.
- The decision reinforces finality as a central organizing principle of civil procedure – litigants are generally entitled to one opportunity to advance their case.
- Pleading *res judicata* is assessed functionally: material facts must be pleaded to provide fair notice, but formal terminology is not required.

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