Revising the Criminal Rate of Interest in Canada

Summary of Recommendations:

1. Lower the maximum rate to an Effective Annual Rate (EAR) of 36%. Ensure that the maximum rate includes all lending costs.
2. Clarify and better enable enforcement. Remove the requirement of an actuarial certificate and approval of the attorney general to prosecute.
3. Repeal section 347.1 which provides an exemption for payday lending.
4. Ensure access to safe and affordable credit for all Canadians.

What is the problem?

The Government of Canada Budget in April 2021 included the following commitment:

Taking Action to Address Predatory Lending

Many lower and modest-income Canadians rely on high-interest short-term loans to make ends meet, such as paying for everyday living expenses, or for unanticipated emergencies. This leaves some Canadians living in a cycle of debt. To help fight predatory lending, the Government of Canada will launch a consultation on lowering the criminal rate of interest in the Criminal Code of Canada applicable to, among other things, installment loans offered by payday lenders.[1]

The 2021 Liberal Party of Canada platform also identified the problem and made a commitment to: *"… crack down on predatory lending by lowering the criminal rate of interest."*

This has been welcome news to many advocates and borrowers. Previous proposals to lower the criminal interest rate in Canada include no less than five attempts, aiming to improve consumer protection and to update this section of the Criminal Code.[2]

Significant changes to payday lending (or high-cost credit) have recently been made within various provinces and yet the harms and proliferation of predatory lending continues.[3] Payday loan interest rates continue to be as high as 500% in most provinces,[4] and a more worrying trend is that installment loans are the fastest growing credit product in Canada, making up the majority of online high-cost loans.[5] In an ACORN Canada study, the percentage of people who took out an installment loan went up by 300% between 2016 and 2020.[6] Federal leadership and action is required to reduce the cost and harm of predatory lenders offering retail credit in Canada.

Who does this issue impact?

Among Canadian families with debt, 4% reported using a payday loan at least once in the past three years, but this number is much higher for people on a low-income, renters, women, Indigenous peoples, and others.[7] Those who do borrow from predatory lenders are often vulnerable, can least afford to borrow, and end up in a cycle of debt. The following demographics are more likely to hold predatory loans:

- Women
- Racialized peoples
- Single-parent households
- People with disabilities
- People living on a low-income
- People on government income assistance programs
- Indigenous peoples
- Tenant households versus home-owning households
- Workers in precarious employment[8]

Almost half (46%) of debtors in an annual bankruptcy study have at least one loan from a payday lender or an alternative easy lender. The average payday loan debt rose 13.0% to $6,534 and the average payday loan size continued to increase, up 9.7% to $1,770. The percentage of high-dollar loans ($2,500 or more) rose to 25% in 2020, up from 21% in 2019 and 15% in 2018.[9]

Among lone-parent households, female-led households are more likely to be at risk. Further, while there are few studies on the issue, available data suggests that there are certain factors that drive the usage of fringe loans among Indigenous peoples including low income, an absence of nearby mainstream financial institutions (FIs), a sense of lack of control over finances held in mainstream FIs, a preference for anonymous finances associated with fringe lenders, poor treatment by mainstream

"I am now borrowing to pay for public transportation to get to work or to cover my rent. It's an endless cycle. It's like being in a tornado and you're just whirling around month after month. It's never a catch-up."

– Patricia

"You're desperate to pay your rent, so you sign… It's easy to get the loan, but that's where the nice part ends, and the financial nightmare begins."

- Sal

"I just knew that they were bad but because I was desperate, I went ahead."

– Dametre

"I couldn't go to the bank to take the loan because my credit score wasn't that good. The government doesn't understand what these loans mean for people because they haven't had to take one."

- Lydia

To learn more about the impact on borrowers see: End Predatory Lending – ACORN members testimonials and High-Cost Alternative Financial Services: The Customer Experience.

FI staff, and inadequate personal identification to access services.[10] Some studies estimate the rate of unbanked individuals in Indigenous communities to be as high as 15%.[11]

Predatory lending not only erodes the financial well-being of individuals, but also families and whole communities. The presence of payday lenders in a community increases the area's risk of poverty and disinvestment. This is in part because wealth is stripped from lower-income households, diminishing their capacity to support local businesses. Money that households could have spent on goods and services in the community goes to service astronomical debt costs instead.[12]

Recommendations & rationale

Given the above context, it is important to end predatory lending in Canada and ensure that every individual has access to affordable credit. The following recommendations have been informed by a coalition of advocacy organizations, academics, community-based organizations, borrowers of high-cost credit, charities and non-profits who have for a long time contributed to or conducted research and advocacy on the negative impact of predatory lenders.[13] If implemented, these recommendations will be the biggest policy shift in our country to finally improve access to safer and more equitable credit.

1. Lower the maximum rate to an Effective Annual Rate (EAR) of 36%. Ensure that the maximum rate includes all associated lending costs: Fines, fees, penalties, insurance, and any related costs.

The Government of Canada defines the criminal rate of interest as 60% EAR and above, through section 347 of the Criminal Code, starting in 1980. A maximum allowable limit is an important indication of our values as a nation and an important policy lever for sustainable lending and economic stability. Seventy-six countries, representing 80% of global GDP and financial assets, impose restrictions on lending rates.[14] Consumer protection concerns are cited as the main reason for the introduction of interest rate ceilings.[15] Quebec has capped consumer lending at 35%.[16] In the US, the 36% rate has been reaffirmed at the state and federal levels in recent years. Congress and three federal agencies have endorsed this rate, and increasingly, the states are capping small loans at 36% or less; currently 15 states and the District of Columbia.[17]

2. Clarify how and who will provide enforcement. Remove the requirement of an actuarial certificate and approval of the attorney general to prosecute a criminal case of interest.

Cases of lenders charging a criminal rate of interest must be clear to identify, pursue, and prosecute. Current requirements present far too great a barrier to identifying and prosecuting a criminal case of interest.

Two important technical changes must be made to section 347 of the Criminal Code to permit appropriate enforcement of violations by Crown prosecutors. The attorney general fiat requirement (subs. 347(7)) and the actuarial calculation requirement (subs. 347(4)) both must be removed. Both are considerable impediments to prosecution of criminal interest rate violations and effectively make prosecution under section 347 impractical and therefore non-existent.[18] In this grey zone of non-enforcement is where the high-cost lending industry grows new products that violate the criminal interest rate.

3. Repeal section 347.1 which provides an exemption for payday lending by transferring responsibility to the provinces. The Criminal Code maximum rate of interest must include all consumer credit in the market today or in the future, including payday lending.

The 2007 decision to exempt payday lenders from adhering to the Criminal Code's maximum interest rate, and the transfer of regulatory responsibility for payday and other high-cost lending to the provinces, resulted in patchwork of inadequate regulation and enforcement across the country and enabled payday loan interest rates to soar, topping 600% in some jurisdictions.[19] Recent reforms to predatory lending in numerous provinces have improved consumer protection but these reforms do not go far enough. For example, changes to the payday loan rules in Alberta have saved Albertans an estimated $10M annually in interest payments. Yet payday lending interest rates still often exceed the Criminal Code maximum. Many lenders have also now turned to promoting installment loans instead of payday loans, which are more profitable to lenders following provincial policy changes.[20]

The repeal of section 347.1 and the consequent re-inclusion of payday loans under section 347 of the Criminal Code should be pursued over a transition period in which the federal government prepares a federally-backed low-income credit product, and supports the creation of safe/affordable alternatives, described in our final recommendation, below.

4. Ensure access to safe and affordable credit for all Canadians.

The Government of Canada must mandate that banks provide access to affordable, small dollar credit.

Introduce a Fair Credit Benefit required under the Bank Act – an affordable loan back-stopped by the Government of Canada

Banking and access to affordable credit is as essential to Canadians as heating and electricity. While many Canadians are struggling financially, banks continue to make record profits.[21] Currently, those who can least afford to borrow in Canada have to pay the most. Banks play a vital role in supporting the financial health of Canadians. However, banks do not presently provide universal access to affordable small dollar loans as an alternative to high-cost credit.[22]

The Bank Act and the Access to Basic Banking Services Regulations outline that banks have a responsibility to make basic banking services available to all Canadians. Many interpret the term 'banking' to mean only basic deposit accounts, rather than a fuller suite of financial services; yet, in Canadian society today, access to a broad range of financial services including credit, is basic. Accordingly, banks must assume greater responsibility for meeting the financial needs of all Canadians—particularly individuals living on a low income—which includes offering safe and affordable credit. Research indicates that if provided with clear, consistent regulations, banks and credit unions can profitably make such loans at prices that are six to eight times lower than those offered by payday lenders.[23]

Support the creation of safe and affordable alternatives

Incentivize, reduce red tape, and enable small dollar credit to be offered in the financial services sectors. Many credit unions are committed to promoting the financial well-being of Canadians, including via affordable and accessible loans. In 2014, Vancity became the first Canadian financial institution to offer an alternative product to payday loans. Now, several other credit unions offer viable alternatives to payday loans.[24]

Canada Post is progressing with their goal to offer affordable credit through postal banking – eventually available at all Canada Post outlets. Canada Post proudly declares they have more outlets than Tim Hortons in Canada, including in rural, remote, and Indigenous communities,[25] and this new initiative is supported by the Canadian Union of Postal Workers.[26]

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