

Criminal interest rate reduced to crack down on predatory lending

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On December 23, 2023, the *Criminal Interest Rate Regulations* (Regulations) were published together with a Regulatory Impact Analysis Statement (RIAS). The Regulations are subject to a 30-day consultation period ending on January 22, 2024. The Regulations build on amendments to the criminal interest rate provisions of the *Criminal Code*, which were introduced as part of the *Budget Implementation Act, 2023, No. 1* in May 2023.

What you need to know

- Currently, all loans are subject to the 60% effective interest rate cap set out in section 347 of the *Criminal Code* without exception. The amendments to the *Criminal Code* are intended to crack down on predatory lending and to help prevent consumers from becoming trapped in a cycle of debt by:
 - moving from an effective annual rate to an annual percentage rate (APR);
 - lowering the criminal interest rate from 60% (which the Government states is equivalent to approximately 48% APR) to 35% APR; and
 - limiting what payday lenders may charge in cost of borrowing to no more than \$14 per \$100 borrowed and limiting dishonoured cheque fees to \$20.
- The Regulations provide exemptions from the new criminal interest rate of 35% APR for certain types of commercial and pawnbroking loans.
- There are exemptions applicable to certain types of loans, which we discuss in more detail.

Commercial loans

The Regulations provide that loans where the borrower is not a natural person and the agreement or arrangement is entered into for business or commercial purposes will be subject to different cap rates depending on the size of the loans. For example:

- loans over \$500,000 will not be subject to any rate cap;

- loans between \$10,000 and \$500,000 will be subject to a 48% APR cap on the interest rate (which is equivalent to the current 60% effective rate cap set out in section 347 of the *Criminal Code*); and
- loans under \$10,000 will be subject to the new 35% APR on the grounds that loans of this size are likely to be made to less sophisticated parties who may be less able to protect their interests or who are at greater risk of being trapped in a debt cycle.

Pawnbroking loans

Pawnbroking loans are loans made by a pawnbroking business to a person who has pawned personal property (other than a vehicle) in exchange for the loan, and that limits the pawnbroker's recourse in the event of the borrower's default to the seizure of the pawned property.

Similarly to commercial loans, different caps also apply to pawnbroking loans: pawnbroking loans under \$1,000 will be subject to a 48% APR limit while pawnbroking loans over \$1,000 will be subject to the new 35% APR limit.

The federal government justified the lower APR cap for pawnbroking loans of a smaller amount on the basis that borrowers are unlikely to be trapped in a cycle of debt given that a pawnbroker's recourse in the event of default is limited to seizure of the goods pawned. In allowing a higher APR limit for loans under \$1,000, the federal government intended to ensure that lenders would not be incentivized to try to get around the 35% APR rate limit by, for example, obtaining pawn licences to offer high-value "collateralized" loans.

Payday loans

The Regulations also introduce a new limit on the total cost of borrowing that may be charged under a payday loan agreement. Currently, the maximum cost of borrowing for payday loans is set by provincial payday loan legislation, which has resulted in limits ranging from \$14 per \$100 in Newfoundland and Labrador to as much as \$17 per \$100 in Nova Scotia, Manitoba and Saskatchewan. The Regulations will limit the total cost of borrowing for payday loans to \$14 per \$100 borrowed. Significantly, the Regulations provide that this limit does not include either (i) a fee, fine, penalty or other charge that is specifically authorized under the applicable provincial payday lending law and imposed on the borrower for default of payment; or (ii) a fee, fine, penalty or other charge for providing a dishonoured cheque or other dishonoured instrument if the amount of the charge is \$20 or less. As noted in the RIAS, the anticipated effect of excluding a dishonoured cheque fee of \$20 or less from the calculation of the total cost of borrowing is that this will cap such fees at \$20.

In summary, the Regulations provide for the following:

Loan type	Loan Amount	Applicable Rate Limit
Commercial	Under \$10,000	35% APR.
	\$10,000-\$500,000	48% APR.
	Over \$500,000	No rate limit.
Pawn loans	Under \$1,000	48% APR.
	Over \$1,000	35% APR.
Payday loan	\$1,500 or less	\$14 per \$100. Dishonoured cheque fee capped at \$20.

Next steps

Members of industry and the public can comment on the draft Regulations until January 22, 2024.

The proposed Regulations would come into force three months following publication of the final Regulations in the Canada Gazette, Part II, and would align with the coming into force of the amendments to the *Criminal Code* to lower the criminal rate of interest. This three-month period would allow lenders to adjust their operations, including IT systems, signage and marketing to align with the requirements.

The Regulations would apply to loans that are entered into on or after the date the Regulations come into force. We note, however, that the new criminal rate does not apply to the receipt of a payment of interest that arises from an agreement or arrangement entered into before the new criminal rate enters into force.

To discuss these issues, please contact the author(s).

This publication is a general discussion of certain legal and related developments and should not be relied upon as legal advice. If you require legal advice, we would be pleased to discuss the issues in this publication with you, in the context of your particular circumstances.

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