

Criminal Rate of Interest

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Pursuant to Section 347 of the *Criminal Code* a criminal rate of interest is defined as an effective annual rate of interest, calculated in accordance with generally accepted actuarial practices and principles, that exceeds 60% of the credit advances. Lenders should be wary of the criminal rate of interest because a loan transaction that provides for a rate of interest exceeding 60% of the borrower could result in criminal charges. Section 347 of the *Criminal Code* makes entering into an agreement or arrangement to receive, or to receive payments for advancing credit exceeding 60% of the total value of the credit advance a criminal offence.

According to the legislation, section 347 creates two criminal charges. Section 347(1)(a) makes it an offence to enter into an agreement to receive interest at a criminal rate and subsection (b) makes it an offence to receive a payment or partial payment of interest at a criminal rate.

Section 347 does not apply to demand mortgages according to the British Columbia Court of Appeal. At the time the parties agree, the mortgage must require a legal rate of interest. However, lenders should be cautious before exercising demand rights. If the loan agreement automatically accelerates the full amount payable on a stated event such as a borrower's default, then the borrower could cause the increase in the effective annual interest rate by defaulting. If the agreement gives the lender the option of demanding repayment in full on the occurrence of the stated event, then the borrower could not alone cause the increase as the lender would also have to act by exercising its option. In this instance, the agreement should not be enforceable by the lender because to enforce the agreement would permit the lender to receive a criminal rate of interest partly as a result of its own act.

The definition of "interest" is quite broad in determining a criminal rate of interest. The definition includes all charges and expenses paid or payable by or for the borrower in return for the advancing of credit. This includes commitment fees, initial fees, loan fees, loan advance fees, facility fees, finance charges, bonuses, capitalized interest, lenders costs, etc. The courts have given a comprehensive definition to protect the public and have said that all charges paid by the borrower for the advancing of credit are included in interest irrespective of the person to whom any such charges and expenses are to be payable. Lenders must be cautious that even if they are receiving interest at less than 60%, the borrower cannot have costs of interest over 60%.

Section 347 applies only to where the loan agreement requires the borrower to pay interest at a criminal rate. Most importantly, the borrower cannot create a criminal rate by its own act of prepaying the loan and shortening its effective term.

The loan agreement cannot include disclaimer clauses that state the parties do not intend the lender to receive a criminal rate of interest. Intent of the parties is irrelevant while determining whether the rate of interest is criminal. It is not relevant that an interest rate over 60% may be an accurate estimate of the lender's risk or that the borrower agreed to pay the criminal interest rate. If found guilty of the offence in section 347, the lender is liable to a term of imprisonment not exceeding 5 years or a fine of up to \$25,000 and imprisonment not exceeding six months.

For any related questions, please contact the writer. To see my previous 1-Minute Reads for Commercial Mortgage Lenders, please visit the Blog portion of my profile at <https://grllp.com/zzlotnick#media-insights>. A PDF version is available for download [here](#).

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