



Memorandum

To: All members of the Canadian Institute of Actuaries and other interested parties

From: Edward Gibson, Chair
Actuarial Standards Board

Kelley McKeating, Chair
Designated Group

Date: May 13, 2024

Subject: **Final Standards: Revisions to Section 4600 of the Practice-specific Standards for Actuarial Evidence – Calculation of Criminal Rate of Interest**

Document 224058m

Introduction

The attached final standards were approved by the Actuarial Standards Board (ASB) on May 8, 2024. It revises Section 4600 of the *Standards of Practice* (SOP) to address a change to the definition of “criminal rate” in Section 347 of the *Criminal Code*. The bill on this change received Royal Assent on June 22, 2023, and is expected to come into force in the coming months.

Background

In December of 2023, the ASB established the Designated Group on Criminal Rate of Interest (DG) to revise Section 4600 of the SOP to address the above-mentioned change to the definition of “criminal rate” in Section 347 of the *Criminal Code*.

A [notice of intent](#) (NOI) was published on January 11, 2024, with a January 31, 2024, comment deadline. Substantive comments regarding the NOI were received from three private lending institutions, three associations (Canadian Bar Association, Canadian Bankers Association and Canadian Lenders Association) and two actuaries. The DG reviewed and considered all comments received subsequent to the NOI distribution and took those comments into account when developing an exposure draft (ED) which was issued on February 29, 2024, with a comment deadline of March 31, 2024.

Comments from stakeholders

Eight comments regarding the ED were received, from:

- two associations (Canadian Lenders Association, Canadian Bankers Association);
- one private lending institution;
- one provincial *Consumer Protection Act* regulator;
- one law firm;

- one association of lawyers; and
- two actuaries.

There continues to be considerable concern among some stakeholders regarding the aggressive implementation timeline. The DG appreciates those concerns, but notes that the timeline for the *Criminal Code* amendments coming into force is outside of its control. The DG's opinion continues to be that it is in the public interest for the SOP formula to be finalized before the *Criminal Code* amendments come into force.

There continues to be confusion regarding the differing formulation and purpose of the SOP annual percentage rate (APR) versus the APR formulas found in the federal Financial Consumer Protection Framework Regulations (FCPFR) and provincial payday loan legislation. The DG appreciates these issues as well. Had the "effective annual rate" (EAR) terminology been retained in Section 347 of the *Criminal Code*, no revision to the SOP would have been required. The DG acknowledges that it is unfortunate that the "annual percentage rate" terminology is now to be used for two different purposes that require different mathematical formulas because of those purposes:

- **SOP APR**, used for purposes of Section 347 of the *Criminal Code*, must take the time value of money into account and must be applicable to both simple and complex loan structures, and both fixed-term and open credit arrangements.
- **FCPFR and provincial consumer protection/payday loan APR** is used for consumer disclosure purposes, generally applies only to relatively simple fixed-term loan structures, and does not necessarily consider the time value of money. Unscrupulous lenders can manipulate the formula's simplicity to produce an artificially low APR.

All of the comments received subsequent to the ED release are summarized and discussed later in this memo. The DG thanks all stakeholders who took the time to comment.

As a result of the various comments received, the DG made two changes to the ED version of Section 4600 before submitting it to the ASB for final approval:

1. The "annual percentage rate of interest" in paragraph 4630.02 is now formally referred to as the "Criminal Code APR" to distinguish it from the FCPFR APR and the provincial APRs. The DG thanks the actuary who submitted this suggestion.
2. In situations where the Criminal Code APR formula yields an APR so close to the criminal rate threshold that different approaches to calculating t_r and t_s (for example) could change the determination of whether or not the rate is criminal, the actuary is now required to so disclose. The DG thanks the actuary who raised this issue.

Due process

The ASB's *Policy on Due Process for the Adoption of Standards of Practice* has been followed in the development of these revisions to the standards.

Effective date and early adoption

These final standards are to become effective on June 1, 2024. Early adoption is permitted if the *Criminal Code* amendments come into force prior to June 1, 2024.

Discussion of exposure draft comments received

Comment re: Need for examples and other support to lenders and consumers

One stakeholder expressed support for a comment in the ED covering memo stating that it would be helpful to see examples of how the SOP APR formula would be applied to open credit products (lines of credit, credit cards, etc.).

Another stakeholder suggested that a tool be developed to permit lenders to input loan parameters to determine whether or not a criminal rate of interest is being charged.

Response

The DG has suggested to CIA staff that a webpage about criminal rate of interest be added to the CIA website, and the CIA has agreed to create such a page. The page will provide definitions and explanations regarding the criminal rate of interest and a directory to assist organizations and individuals in search of an actuary with expertise in criminal rate of interest issues. The CIA advised that the new webpage may be available before the end of 2024.

Given the wide variety of loan structures in existence, the DG is of the opinion that an online tool may give some lenders false comfort regarding the Criminal Code APR that their product is charging as a result of incorrect data input or their having a loan structure that does not properly fit into the tool parameters. The DG believes that the CIA webpage being developed will be a more appropriate educational resource for both consumers and lenders.

Comment re: Educational note

An actuary suggested that an educational note, with examples, would be helpful due to the wide range of loan structures in existence.

Response

The DG will bring this suggestion to the attention of the Actuarial Evidence Practice Committee.

Comment re: “Days-based” calculations

One actuary and one association reiterated an earlier observation that the current SOP does not prescribe the specific approach for determining the time periods between payments advanced and repaid (t_r and t_s in paragraph 4630.01 of the SOP): exact days, 365-day year, 366-day year, exact length of month vs. months are one-twelfth of one year, etc. The actuary noted that different actuaries could calculate slightly different EARs under the EAR formula and could also calculate slightly different APRs under the proposed SOP APR formula and suggested that a specific approach for counting days be prescribed.

Response

The DG continues to be of the opinion that it is preferable to leave the definitions for t_r and t_s as they currently stand in order to best accommodate the wide range of fixed-term and open credit loan structures.

To address this concern in another way, the final standard now includes a requirement that, in situations where the Criminal Code APR formula yields an APR so close to the criminal rate threshold that different approaches to calculating t_r and t_s would alter the determination of whether or not the rate is criminal, the actuary is required to so disclose.

Comments re: Timeline to finalize the SOP

Several stakeholders expressed concern over the implementation timeline and suggested additional consultation regarding the proposed formula.

Response

The DG anticipates that the amendments to the *Criminal Code* (with associated regulations) may come into force in the coming months. Although the DG appreciates concerns regarding the implementation timeline, the coming into force date is outside of the DG's control. The DG's opinion continues to be that it is in the public interest for the SOP formula to be finalized before the *Criminal Code* amendments come into force.

Stakeholders who wish to advise the federal government of concerns regarding the timeline for bringing the *Criminal Code* amendments into force should contact Mark Radley, Director, Consumer Affairs, Financial Sector Policy at Finance Canada (mark.radley@fin.gc.ca). Mr. Radley has authorized the DG to share his contact information.

The ASB disseminated the NOI and ED to a large number of stakeholder groups, and those stakeholder groups had the opportunity to further circulate the NOI and ED to their contacts. Given the number and nature of comments received, the DG is satisfied with the breadth and depth of input provided to the ASB's due process for revisions to the SOP. Due process regarding consultation has been followed.

Comment re: Complexity of the SOP APR formula

One stakeholder indicated that the method for calculating the SOP APR should be more understandable.

Response

The purpose of the SOP APR formula is to determine whether or not a lender is charging a criminal rate of interest. The proposed SOP APR formula is based on the existing formula for EAR. Organizations that are currently assessing their loan and credit arrangements for compliance with Section 347 of the *Criminal Code* should not encounter significant hurdles in modifying that assessment process to the new SOP APR formula.

The SOP APR formula is not intended to assist consumers or commercial borrowers to compare the costs of various alternative loans. Instead, the SOP APR formula is intended to permit lenders, borrowers, regulators and the courts to determine whether or not a specified loan arrangement (fixed-term or open credit) is charging a criminal rate of interest. The SOP APR would not normally be disclosed to borrowers, except at the lender's discretion. It does not change or replace the FCPFR APR formula or disclosure rules, nor does it change or replace the various provincial APR formulas and disclosure rules.

Comments re: Comparability to FCPFR or provincial APR formulas

One stakeholder observed that the SOP APR formula is different from the FCPFR and/or provincial APR formulas.

Another stakeholder suggested that the SOP APR formula does not properly account for the time value of money, when the opposite is actually true.

Response

The reasons for the divergence between the SOP APR formula and the other APR formulas were discussed extensively in the ED covering memo. Of key importance:

- The FCPFR and provincial APR formulas do not correctly account for the time value of money. Whether a broker fee (for example) is payable at the beginning or the end of a fixed-term loan

period has no impact on the provincial APR because the time value of that fee is not taken into account in the provincial APR calculation.

- In contrast, the SOP APR formula does take the time value of money into account. The loan structure that requires the broker fee to be paid at the beginning of the term will result in a higher SOP APR, all other things being equal. This is a strength, not a weakness, of the SOP APR formula.

“Coming into force” date for the *Criminal Code* amendments

Since the “coming into force” date for the *Criminal Code* amendment is not yet known, paragraphs 4610.02, 4630.01, and 4630.02 of the revised Section 4600 refer to “the coming into force of Sections 610 to 612 of the Budget Implementation Act no. 1 2023.” After the actual “coming into force” date is known, the ASB will amend paragraph 4610.02 to replace this phrase with the actual effective date. Since this change would be a minor revision (as that term is defined in ASB due process), the DG’s understanding is that there would not be a public consultation on that change.

Members of the DG

The members of the DG were Kelley McKeating (Chair), Greg Gillis, Jay Jeffery, Jamie Jocsak and Marshall Posner.

The DG wishes to acknowledge and thank Thierry Chamberland, who performed the technical review to ensure that the French version of the revised Section 4600 is consistent with the English version. The DG also thanks the ASB for its guidance, the Actuarial Evidence Practice Committee for its comments and CIA staff for their assistance.

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