

# Regulatory Impact Statement

## EXECUTIVE SUMMARY

The current law providing for payment of interest where there is late payment of money owing, is limited, not easily accessible, relies to some extent on judicial discretion, and fails to adequately compensate many creditors. A single, comprehensive and more widely applicable Interest on Money Claims Act is needed, with a basis for interest that reflects the commercial value of delay in payment of money owing. The proposed Act is based on the Law Commission's report *Aspects of Damages: The Award of Interest on Money Claims* (NZLC R 28, 1994), updated in 2007. The proposed Act will provide fair compensation for creditors, will deter litigation and will include a method of calculation of interest that is administratively simple and predictable.

## ADEQUACY STATEMENT

The Ministry of Justice has reviewed this regulatory impact statement and considers that it fulfils the adequacy criteria.

## STATUS QUO AND PROBLEM

The current statutory law provides limited exceptions to the restricted common law approach to payment of interest on money claims. The general law varies according to whether a claim is pre-judgment or post judgment or is as of right. The statutory prescribed rate is a fixed simple interest rate but allows judicial discretion to reduce the rate. The prescribed rate lacks flexibility, particularly at times of change in market rates. A claim at common law is also limited and dependent on judicial discretion, and is currently in a state of change.

The current law can also mean inadequate compensation for creditors. The uncertainty and complexity of the law can lead to excessive litigation and unnecessary costs in judicial and court time, as it is not possible for practitioners to predict outcomes of claims.

## OBJECTIVES

The objectives of the proposed Interest on Money Claims Act are:

- Simplicity, accessibility and predictability of the law,
- adequate, commercially realistic, fair compensation for creditors, and
- a method of calculating interest owed, using a published interest multiplier that is updated regularly and administratively, and is easy to use.

The appropriate rate of interest to reflect the cost of delay in payment should be:

- regularly published and easily ascertainable,

- reasonably stable,
- balanced between a standard borrowing rate and a standard lending rate,
- based on a term that corresponds roughly to the average period that money is outstanding,
- free from irrelevant risks.

## **ALTERNATIVE OPTIONS**

### *A single Interest on Money Claims Act with fixed interest*

The option of a single Act for all claims of interest on money judgments, but retaining a fixed rate of interest was considered, but does not accord with the reality of the commercial loss when payment of money owed is delayed. A fixed statutory rate also requires government review and intervention by regulation in order to change the rate.

The above option including wide judicial discretion was discarded as encouraging litigation.

The above option of a fixed rate of interest with no or very limited judicial discretion, and the option of retaining simple interest, were both discarded likewise, as being inadequate in the light of market reality. Adequate compensation requires compound interest and adjustable rates.

### *Interest option based on borrowing rates*

Options for a base rate of compound interest were explored in NZLC R 28 using first, borrowing interest rates, and secondly, lending (investment) interest rates. It was concluded after consultation that a borrowing rate could over-compensate a creditor. Lending interest rates would be a fairer basis in general, providing a greater encouragement to debtors to pay as they are lower rates. Realistically, debtors are less likely to have the resources to pay at borrowing interest rates, and this would more likely lead to litigation, and the use of court time and costs in debt collection.

### *Appropriate indicator or base rate options*

Of the rates considered for the 1994 report, the first mortgage housing rate and average base lending rate are now discarded as borrowing rates (see above). The lending rates considered were the call rate, discarded as liable to be affected by seasonal and short term political considerations, the two-year government stock yield rate and the 90-day bank bill rate.

Of the latter two lending rates, the option of the 2 year government stock rate, originally proposed by the Law Commission in 1994, was preferred at that time as reflecting a longer term investment and being relatively stable and exposed to limited risk factors. However, it is now not recommended by the Law Commission as it is less liquid than in 1993 and not available on a daily basis without interpolation, so is less accessible than some other rates.

## **PREFERRED OPTION**

### *A single Interest on Money Claims Act providing for compound interest*

The preferred option is for an Interest on Money Claims Act as a single statute providing for all interest on money claims, as of right (with a few specific exceptions). Interest will be compounded, based on the official cash rate, and calculated by an interest multiplier published on the Ministry of Justice High Court website.

The option of an Interest on Money Claims Act is preferred because of:

- its legal simplicity and ease of access,
- its fairness to creditors and commercial realism (allowing fluctuating, compound interest so it will encourage the confidence of the commercial community).

A multiplier for interest calculation is preferred as it limits judicial discretion and is predictable, so it will deter litigation and judicial involvement, and reduce court costs. It will be accessible and easy to use so will save time and resources.

### *Appropriate base interest rate*

The official cash rate is preferred as a base interest rate because it is regularly reviewed by the Reserve Bank Governor, is reasonably accessible to individuals and is reasonably stable.

### *Retaining common law claims*

The Act would not bar common law claims, but the statutory route will be generally preferable to the common law which is in a state of flux and uncertainty and requires proof of loss.

### *Resources required*

It is necessary initially to draw up an interest multiplier, and to keep this updated and posted on the High Court website. The Law Commission and the Ministry of Justice have commissioned a pilot multiplier that calculates (using Microsoft Office Excel) interest owing at variable dates and variable rates, based on the Reserve Bank's official cash rate plus a margin. The interest multiplier also provides an easy method for ascertaining interest owing where instalments have been paid over time, and has simple instructions for the court registrar updating the base rate.

Minimal resources will be required by the Ministry of Justice for the court registrar to update the base rate on the interest multiplier when updates are announced by the Reserve Bank. But these resources should be easily off-set by savings in court time from ease of calculations and decreased civil litigation (due to the predictability of the outcome of a case and limited judicial discretion).

## *Amendment of statutes and regulations*

The preferred option will replace some existing legislative provisions that will need to be repealed (section 87 of the Judicature Act 1908 and section 62B of the District Courts Act 1947), and it will require the amendment of some statutes and regulations. The preferred option will not override existing specific statutory interest regimes such as that in the Injury Prevention, Rehabilitation and Compensation Act 2001 (section 114) and the Life Insurance Act 1908 (section 41A),<sup>1</sup> except as to the base interest rate.

Other statutes requiring consequential amendment are: the Companies Act 1993 (section 309), District Courts Act 1947 (section 77(2)(b)), Employment Relations Act 2000 (clause 11 of schedule 2 and clause 14 of Schedule 3), Holidays Act 2003 (section 84(3) and (4)), Insolvency Act 2006 (sections 253(2) and 267), Land Transfer Act 1952 (section 235(3)(a)), Maori Reserved Land Amendment Act 1997 (section 23(2) and clauses 8 and 25(3) of Schedule 1), Prisoners' and Victims' Claims Act 2005 (section 47(3)), Retirement Villages Act 2003 (section 70(1)(c)), and Weathertight Homes Resolution Services Act 2006. A number of regulations will also require consequential amendment, and separate amendments will be required for the High Court Rules and District Courts Rules 1992.

## **IMPLEMENTATION AND REVIEW**

There will be liaison with the Ministry of Justice court registrars concerning the implementation of the new Act. The Ministry of Justice will advertise the new system and the interest multiplier on its court website.

## **CONSULTATION**

The Law Commission consulted widely in 1994: see the cabinet paper and appendix H of NZLC R 28.

During the period of updating its recommendations in NZLC R 28, in August to October 2007, the Law Commission has consulted The Rt Hon Justice Peter Blanchard of the Supreme Court, who was a Law Commissioner responsible for NZLC R 28 in 1994, the Government Actuary, the Governor of the Reserve Bank, Parliamentary Counsel Office, the Inland Revenue Department, the Ministry of Justice, the Treasury, the Department of Labour, the Ministry of Economic Development, Land Information New Zealand, Te Puni Kokiri, the Department of Building and Housing, the Department of Internal Affairs, and the New Zealand Law Society.

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<sup>1</sup> In its report *Life Insurance* NZLC 87 (2004) the Law Commission recommended that section 41A of the Life Insurance Act 1908 be amended to provide that the rate of interest payable on claims paid after 90 days following the insured's death be the Reserve Bank 90-day bank bill rate; this was in order to remove the incentive for delay by insureds under the present system (interest is at a rate stipulated in the policy or prescribed by the Judicature Act 1908). An interest rate based on the official cash rate should have the same effect.