

Surprise *decrease* to the penalty interest rate

After remaining stable at 12% since 2006, last week the Victorian State Government announced that the official penalty interest rate will decrease to 11% per annum from 1 September 2008.

This may be relevant to clients with contracts containing payment provisions and a deterrent obligation to pay interest on late payments. These commonly refer to this rate, set by the Attorney General under section 2 of the Victorian *Penalty Interest Rates Act 1983*.

It is a surprising move, since over the same period the Reserve Bank's cash rate target has increased by 1.00% pa (even taking into account the 0.25% reduction earlier this week). If anything, we would have expected the penalty interest rate to increase at a similar rate.

For future arrangements, at least when acting for the party likely to receive payments, it is suggested that the margin be increased to compensate – for example agreements which previously provided for a penalty interest of 2% above the set rate could now provide for, say, 3%, maintaining an effective rate of 14% pa.

Of course, this tactic is usually not possible for agreements already in effect – parties owed amounts under existing agreements will now be at a disadvantage, as unscrupulous debtors may prefer to incur penalty interest under the agreement to paying higher rates on their overdraft or credit card.

For further assistance, please do not hesitate to contact Paul Stephens, Cathy Drake, Kent Mallinson or Rebecca Hanley in the Nevett Ford Commercial Law Ballarat Department.

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