**Wider Review of Scotland’s Statutory Debt Solutions**

**Stage 2 Working Groups – Summary of Issues and Recommendations**

**March 2022**

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# Working Group 1 – Moratorium and Common Financial Tool

| **Issues Discussed** | **Outcomes/Recommendations** |
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| **Moratorium – Issues**  The existing moratorium provides for a six week (42 day) period within which someone can seek advice on problem debt – during this time creditors are prevented from taking recovery action. There is no requirement for a money adviser to be involved in the process.  The working group has discussed issues relating to the length of the moratorium and whether features that have been included in the more recent “Breathing Space” Scheme in England and Wales should be incorporated – these include:   * Money adviser involvement in the application * Protection period of 60 days * Freezing of interest and charges during the period * Separate criteria and flexible duration of protection for those experiencing mental health crisis | **Moratorium – Recommendations**  The group believe neither the six week period nor the six month period are appropriate for the longer term. They could not agree on an alternative moratorium period.  They consider an option should be introduced for extension of up to 30 days for very limited circumstances beyond the applicant’s control (more controversial amongst creditors) and that if this were done, the most appropriate timescale would be a standard period of 60 days to align with the rest of the UK.  There is an acknowledgement that clarification would be required on possible additional protections - such as preventing repossessions - if the extended option is made available. Therefore, the impact of this option may require more detailed investigation and form part of Stage 3 of the review.  Interest and charges should be frozen from the outset of the moratorium period.  Mental health crisis provisions should be implemented in Scotland – requires more detailed investigation and is possibly more appropriate for Stage 3 of the review.  With the possible introduction of any additional protections, money advisers should be involved from the outset – although it was recognised that this would create additional workload for the sector. |
| **Common Financial Tool – Issues**  The Common Financial Tool (“CFT”) in Scotland is the statutory method that is used in assessing income and expenditure (and surplus income available to make contributions) in statutory debt solutions.  The tool defined in legislation is currently the Common Financial Statement (“CFS”) which is used by advisers under license from the Money Advice Trust.  The working group has considered the merits of the current tool (CFS) as compared with (i) the alternative income and expenditure tool used more widely across the UK (the Standard Financial Statement – developed by the Money and Pensions Service) and (ii) Alternative models used in other overseas jurisdictions, including an assessment made only on the level of income. | **Common Financial Tool – Recommendations**  The group has considered several models in operation in other countries and modelling that has been undertaken to examine what the likely impacts would be to those that have entered debt solutions here.  There is no clear consensus on the most appropriate solution. The income and expenditure model provides for the most accurate assessment of individual circumstances, whereas the income only based model provides for easier administration with analysis showing a better outcome in terms of retained income for those in the solution – although this is not always the case.  Analysis shows that around 15% of Scottish bankruptcies following a debtor application result in payment of a contribution. It is estimated that the application of the income based approach used in Australia would have resulted in only 2% of the cases paying a contribution. In contrast, estimates are that the income based approach used in Ireland would have resulted in a contribution in 58% of those cases.  The preferred options for recommendation include:   * Retaining the income and expenditure model – with reform to allow more flexibility on the use of full surplus income being taken towards repayment. This would promote financial resilience and rehabilitation. * Adopting an income based approach - with income set at the right level to represent a fair balance between the interests of debtors and creditors.   Regardless of the type of model implemented, there was a consensus from the working group recommending that the full surplus income no longer be taken as a contribution. Instead, either:   * a percentage of the surplus income is taken as a contribution (e.g. 50%); or * a set figure is automatically excluded from the surplus and the remaining amount is taken as a contribution (e.g. the first £75 is excluded). |

# Working Group 2 – Protected Trust Deeds

| **Issues Discussed** | **Outcomes/Recommendations** |
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| **Impact of Protected Trust Deed (“PTD”) Protocol**  The group has focused on the issues raised by the then Economy, Energy and Fair Work Committee (“the Committee”) during its PTD Inquiry, conducted in January 2020. This wider policy review is the first recommendation of the Committee – albeit that it couldn’t complete during the last Parliamentary session due to the pandemic.  The Committee inquiry and recommendations centred on concerns that have been raised in relation to PTDs – particularly from (i) creditors, due to the high costs/low returns and perceived mis-selling of the solution and (ii) money advisers, based on the poor outcomes for debtors where the solution is unsustainable and fails.  Since the inquiry published its report, work has been taken forward to develop a voluntary protocol to address, at least in part, the Committee’s recommendations in the following areas:  i. Earlier dividend payments to creditors  ii. Improved protection where a debtor’s discharge is refused  iii. Ensuring that trustees (Insolvency Practitioners (“IP”)) only accept referrals from Financial Conduct Authority (“FCA”) regulated organisations.  The protocol has now been adopted by a number of IPs and, importantly those that represent the high volume firms. This will mean that 75-80% of future PTDs will be offered by protocol compliant trustees. | **Impact of PTD Protocol - Recommendations**  The group has broadly welcomed the protocol that has been put in place – the Institute of Chartered Accountants of Scotland (one of the Recognised Professional Bodies) has expressed concern over the protocol due to its voluntary nature and lack of legislative enforcement.  The recommendation is that the protocol is allowed to run for a reasonable period before the impact is fully assessed – it has the potential to address, at least in part, five of the Committee’s recommendations (2, 3, 4, 5 and 11 as set out in paper 3 titled Wider Review of Scotland’s Statutory Debt Solutions).  Legislative options can be further reviewed in light of the evidence obtained through the operation of the protocol. |
| **Minimum Debt Level**  The group has considered the issues associated with the Committee’s recommendation (number 12 as set out in paper 3) to increase the minimum debt level required to enter a trust deed – this currently stands at £5,000. In addition, they have discussed the Committee’s suggestion that an additional debt product be investigated.  The primary issues involved can be summarised as:   * The creditor returns in lower debt level PTDs are more significantly impacted by the level of administrative costs applied * The contributions typically paid in lower debt level PTDs and the resultant total payments during the PTD raised questions as to whether a PTD was the appropriate solution from both the debtor and creditor perspectives   The issues here are complex as moves to intervene on minimum debt level and access to PTDs as a means of debt resolution impinge on other areas such as individual choice and the basic position that trust deeds are voluntary in nature with legislative provision in place for creditor consent (through voting) and protection. | **Minimum Debt Level – Recommendations**  This remains a contentious issue with sharply opposing views – particularly amongst the creditor (predominantly small creditor) and IP stakeholder groups.  The group has drawn on a range of statistical data to assess the impact of any increase  in minimum debt level and the likely number of cases impacted and also data on lower debt level PTDs showing the period of time within which the repayments would repay the debt in full (indicating those cases that may be more appropriately suited to Debt Arrangement Scheme (“DAS”)).  The statistical analysis has also shown some positive progress since the reforms introduced to DAS in late 2019 – the firms operating in the high volume PTD market are now amongst the most active in DAS. This is as consequence of the funding reforms introduced which has resulted in DAS featuring amongst the solution tool-kit of more organisations. The group has noted the following:   * The proportion of total PTDs with debt levels of less than £6,000, £7,500 and £10,000 show a decreasing trend in each of the years subsequent to 2018/2019 * The proportion of total PTDs where the contributions can pay the total debt in 54, 60 and 72 months show a decreasing trend in each of the years subsequent to 2018/19 * DAS activity levels have increased since the 2019 reforms – in contrast to the trends seen for other insolvency solutions   Notwithstanding these developments, the working group has not reached a consensus on this issue and while the arguments and analysis will be set out in their findings, it is likely that it will call on Ministers to make a judgement call. The group is clear that any consideration of a new mechanism should be considered at the Stage 3 of the review. |
| **Improving Information and Debtor Understanding**  The group discussed two Committee recommendations (7 and 9 as set out in paper 3) which centre on the importance of debtors being fully informed of options before entering a solution. This suggestion involves the development of a clear and easily accessible information leaflet setting out the benefits and risks of entering a PTD.  The option of a “cooling off” period has also been considered – the suggestion is that this would apply between a debtor receiving the information leaflet and signing a trust deed. | **Improving Information and Debtor Understanding – Recommendations**  Agree that it is critically important that a debtor receives the right amount of information in order for them to be able to make an informed choice on the option which best suits their individual circumstances.  A draft PTD information leaflet would be useful starting point in improving transparency – while recognising that debtors can receive large volumes of information at the present time. A draft leaflet has been produced containing what the group considers to be the key information on benefits and risks and this will be included in its report. Further consideration is required in order to future proof the information made available to consumers – for example using technology and social media in order to better reach people who need help.  It was suggested that the Scottish Government do more to raise awareness of all statutory debt solutions.  Although a “cooling off” period would bring trust deeds into line with other complex financial products, the group acknowledged the difficulties in implementing this provision in trust law and agreed that this should not be pursued within the Stage 2 review. |
| **Pre-Trust Deed Free Independent Advice**  The group considered the linked recommendations (numbers 6 and 8 as set out in paper 3) of the Committee Inquiry concerning the provision of free independent advice for individuals prior to them granting a trust deed and the associated resourcing issues that would be created by reforms of this nature.  Evidence given during the Committee Inquiry and further stakeholder feedback highlighted concerns over the extent to which some individuals with problem debt are being “mis-sold” a PTD in favour of an alternative solution better suited to their needs and the interests of the creditors involved.  Examples were given of circumstances where PTDs failed because they were neither viable nor sustainable having no sound financial basis on which to proceed at the time of application.  There is an existing legal requirement for a debtor to have received money advice before they enter a statutory debt solution. Free sector money advisers can provide this for bankruptcy and DAS. However, it is usually an insolvency practitioner (or someone who works for them) who provides this advice prior to the granting of a trust deed. This issue concerns the additional involvement of an independent adviser in these cases. | **Pre-Trust Deed Free Independent Advice – Recommendations**  The general view is that it is not currently feasible to have pre-trust deed advice provided exclusively by the free money advice sector due to lack of available resource to meet potential demand.  The working group recognise that the free advice sector faces significant pressure and the demand is likely to increase as the full economic consequences of the Covid pandemic are felt amongst consumers.  Most DAS applications are now instigated through private sector organisations. This suggested that the mandatory requirement for free sector advice prior to the granting of a trust deed would create inconsistency with DAS.  The group does not recommend the mandatory requirement for free independent advice. The provision of high quality advice by appropriately skilled people in advance of entering any debt solution is of critical importance - irrespective of the whether this is provided through the free, charitable or fee charging advice sector  Future resourcing of free advice is an important consideration for the Scottish Government and this should be one of the clear priorities linked to the delivery of the Debt Advice Routemap. As set out by the Committee, this work should include exploring alternative models to resource the sector and ensure that the capacity exists to meet future demand and that the advice needs of those facing issues of problem debt are met. These funding issues are considered beyond the scope of the wider review of statutory debt solutions. |
| **Implications of Debtor’s Death During a PTD**  The group considered the recommendation of the Committee Inquiry to consider if PTD arrangements strike the appropriate balance between creditors and family members when death occurs during a PTD (recommendation number 13 as set out in paper 3).  The agreement between the debtor and the creditors, which forms the basis of the PTD ends on the death of the debtor. This means that the estate of the deceased debtor becomes liable for payment of all their debts in full (if sufficient estate is available). In addition to the original sum included in the PTD, creditors are entitled to interest at the prescribed rate where funds are available. IPs can also charge additional fees for work done in realising any assets. If the deceased debtor owned a home, this will often need to be sold to pay the debt. This could effectively mean the estate has to pay out much more than the value of the person’s original debt, reducing the amount of funds available to pay beneficiaries in any inheritance. | **Implications of Debtor’s Death During a PTD – Recommendations**  The group discussed the current process that applies where a debtor dies during insolvency and also considered succession and partnership law and the statutory processes that apply on death in a non-bankrupt estate.  The same duty to settle debts ahead of recognising any entitlement of beneficiaries to the estate applies consistently whether there is a solvent or insolvent estate.  Having considered these areas of bankruptcy, succession and partnership legislation, the group agreed that the repayment of debt to creditors ahead of beneficiaries from a deceased estate is well established in different areas of the law. The clear recommendation is that no changes are required to this existing principle in the PTD process.  The group recommended that the Scottish Government publication “What to do after a death in Scotland” be updated to include the requirement for an executor to check the Register of Insolvencies and the DAS register before distributing funds to beneficiaries. |
| **Prescribed Rate of Interest**  The group discussed the recommendation from the Committee Inquiry concerning the current 8% prescribed rate of interest (number 14 as set out in paper 3). | **Prescribed Rate of Interest – Recommendations**  The group recognised that consideration of this issue was best progressed by working group 3 – in recognition of the cross-cutting nature of the rate of interest applying in statutory debt solutions. |
| **AiB Audit Activity – PTDs**  The group discussed the recommendation from the Committee Inquiry requesting that AiB increase self-initiated audits to monitor and discourage potential poor practice, and  publish any trends found (number 10 as set out in paper 3). | **AiB Audit Activity – PTDs – Recommendations**  The group made no recommendation here. They consider this is a matter for AiB. The reformed fee structures introduced in 2013 has reduced the scope of action being taken on trustees’ remuneration as part of the audit process – although action could be taken on inappropriate outlays charged to the case. The group highlighted the additional administration costs arising from trustee, creditor or debtor led audit requests. |
| **Debtor Discharge and Refusal of Discharge**  Under the principles of trust law if a trust deed contains a clause to allow it to be brought to an end in return for part payment of the debt then it will be competent for an offer of composition to be made and agreed with creditors in a trust deed.  There is, however no provision in the current PTD legislative process for obtaining the early discharge of a debtor or trustee in a PTD prior to the completion of the 48 month contribution period (aside from when all debts are paid in full). This includes an offer of composition to be made to creditors.  The PTD legislation allows for a trustee to refuse to apply for the debtor’s discharge (normally because of non-cooperation) however, this is only following a request for discharge by the debtor or after the end of the repayment period. A debtor can appeal this decision to the Sheriff Court.  The issues considered are whether statutory provision should be introduced to allow for the early discharge of a debtor in specific circumstances and to remove the time limitations on the refusal of discharge process. | **Debtors Discharge and Refusal of Discharge – Recommendations**  Rather than creating a new provision, the previous composition process outlined in schedule 4 of the Bankruptcy (Scotland) Act 1985 (“the 1985 Act”) (pre revisions in 2008) should be introduced with consideration given to current legislative processes. Creditors should firstly be presented with the proposal and if they do not all agree, AiB would adjudicate on it through a “fair and reasonable test”.  A new provision should be introduced to allow debtors who can no longer make contributions to their PTD to be discharged from their PTD at any stage in the process. This will only be considered in specific circumstances and again creditors should firstly be presented with the proposal and if they object AiB would adjudicate on the case.  Time limitation on the refusal of discharge process should be removed from legislation allowing the trustee to initiate refusal of discharge at any time. The debtor should have recourse to challenge this. However, this should lie with AiB not the Sherriff Court to simplify the process for the debtor. |

# Working Group 3 – Bankruptcy and wider issues

| **Issues Discussed** | **Outcomes/Recommendations** |
| --- | --- |
| **Bankruptcy Debt Thresholds**  The group has considered the entry parameters that apply to debtor application led bankruptcy – particularly the debt thresholds that govern entry criteria.  It has also considered the creditor petition debt level that applies in court instigated processes.  For Minimal Asset Process (“MAP”) bankruptcy the minimum debt level is £1,500 and for both Full Administration debtor application and creditor petition bankruptcy the level is £3,000. MAP bankruptcy involves a maximum debt level of £25,000 – recently increased from £17,000 through amending Regulations. | **Bankruptcy Debt Thresholds – Recommendations**  The group has considered a range of statistical information on the impacts of amending the debt thresholds.  The minimum debt level for MAP bankruptcy should be removed. There was consensus on this, as the introduction of mandatory debt advice provided protections for those seeking bankruptcy for unreasonably low levels of debts. The group recognised that for those with no means to repay small levels of debt, bankruptcy could be the best option and access to this form of debt relief should not be denied. A MAP bankruptcy is a quick process and would allow a person a fresh start more quickly than any other alternative.  There is no consensus on whether to remove the minimum debt level or whether to maintain the £3,000 level for Full Administration bankruptcy. They recognised that increasing the threshold could have a detrimental effect on clients with difficult debt issues and reduce the solutions available. The group considered the merits of removing the threshold and while some supported this others recognised that having a minimum debt threshold provides some protection against those with relatively low debt levels taking the serious step of entering bankruptcy. Ultimately, if there has to be a minimum debt level, there was agreement this should be retained at £3,000.  There was general consensus that the maximum debt threshold for MAP is retained at £25,000. This would enable further assessment of the impact of the recent increase before considering further adjustment.  Having considered the impact of revision, the minimum qualifying creditor debt level required to give rise to creditor petition bankruptcy should increase from £3,000 to £5,000. This level is considered to strike a fair balance between the interests of creditors and debtors and is consistent with the rest of the UK. |
| **MAP Bankruptcy Asset Thresholds**  The group has considered the asset thresholds that govern entry criteria for debtor application MAP bankruptcy.  The prescribed limits applying to MAP eligibility are that total assets must not have a total value in excess of £2,000 and no single asset owned should be valued in excess of £1,000. This excludes a vehicle with a value not exceeding £3,000 where there is a requirement for use. | **MAP Bankruptcy Asset Thresholds – Recommendations**  A broad range of statistical information has been considered in relation to the assets held in cases entering both MAP and Full Administration bankruptcy.  The group recommend that there should be an overall asset threshold for entering MAP bankruptcy – there is no apparent rationale for providing separate provisions for individual and total assets. No amount was agreed and further consultation is required to determine an appropriate level.  Expert opinion should be sought on what the reasonable average value of a modern mid-sized family car would be - for consideration at stage 3 of the review. The statutory asset value for a car should be amended to take account of this assessment. Work should also be carried out through guidance to improve consistency in approach when dealing with vehicles. The outcome of this assessment should apply to the treatment of vehicles by trustees in bankruptcy. Further consideration should be given to how disability vehicles are treated.  There should be specific exclusion of mobility scooters from the asset value to remove any confusion. These are disability aids and essential for those who use them. |
| **Repayment periods in Debt Solutions**  The issues considered here include:   * Current repayment periods in DAS * Current repayment periods in bankruptcy | **Repayment periods in Debt Solutions**  The flexibility over the duration of DAS Debt Payment Programmes (“DPP”) should be retained. This would prevent individuals being forced into bankruptcy or a PTD where another option acceptable to creditors is available.  It is important for advisers and those with debt to consider the viability and sustainability of the DPP at the outset as there would be no benefit and potentially significant detriment in embarking on a programme that could not be completed.  The group recommends that the repayment period in Full Administration bankruptcies is reduced to three years. While the statistics demonstrate a small increase in dividends for creditors with the four year repayment period, this needs to be balanced against the additional contributions required to be made by debtors. The group agreed this small increase did not justify retaining the longer contribution period and the repayment period should revert to three years.  The group was not able to reach consensus on the acquirenda period for MAP or Full Administration bankruptcy and whether these should be aligned. In MAP there were concerns that a four year acqurenda period was excessive, putting an unreasonable burden on debtors, however, there was also recognition that it is reasonable that creditors can obtain a further return in dividends where post-bankruptcy assets are identified. The group agreed, however, that there should be no option to re-open a MAP bankruptcy in order to recover income contributions. In Full Administration bankruptcies there was agreement that aquirenda was appropriate and further consideration should be given to whether this should be set at three or four years and whether it should be aligned with discharge. |
| **Exit from Solutions**  The issues considered here include:   * Current composition arrangements in DAS * Implications of deceased debtor in DAS * Composition in bankruptcy * Bankruptcy discharge process specific to uncooperative and untraceable debtors | **Exit from Solutions – Recommendations**  The existing composition arrangements for DAS (broadly admissible after 12 years repayments and repayment of 70% of debt) are considered too stringent and should be reformed - very few cases have yet qualified.  There should be further consultation on this issue – seeking views on composition following a seven year repayment period with a prescribed percentage of debt repaid.  Where a DAS is revoked in the case of a deceased debtor, the processes on the retrospective application of interest and charges should be revised and removed. There should be distinction between revocation in these circumstances.  Re-introduction of composition in bankruptcy with the eligibility criteria and processes modernised and streamlined. This should be an AiB rather than a court process, with creditors having the right to request a review and where necessary appeal through the court. Creditor consent criteria should be determined.  The group recommends that trustee discharge should not be linked to debtor cooperation.  The group believed that the current situation where discharge is deferred indefinitely due to non-cooperation is not appropriate. They recommend that further consideration should be given as to whether delayed discharge (with an agreed end period) or the use of Bankruptcy Restriction Orders (“BROs”) are more appropriate for dealing with non-cooperation.  Consideration should be given to closing a case where a debtor has not been traced within a set timeframe (five or seven years). There should also be a revised mechanism and timescale in place to allow these cases to be returned to AiB.  Consideration should be given to explore further whether there is now a case for extending composition to Business DAS – this should take account of a partial settlement proposal which is built into Business DAS. |
| **Prescribed Rate of Interest**  Bankruptcy legislation prescribes the interest rate that may be payable to creditors on the conclusion of insolvency proceedings where sufficient estate remains after payment of relevant expenses and the full settlement of preferred and ordinary debts. In these circumstances interest is payable from the date of bankruptcy to the date of payment of the debt. This is known as the prescribed rate of interest (often referred to as the statutory rate of interest). The prescribed rate of interest is the greater of:   * the prescribed rate at the date of sequestration, or * the rate applicable to that debt apart from the sequestration (i.e. the agreed contractual rate of interest).   Where a court decree for payment includes interest or states that interest is payable this is the judicial rate of interest.  Both the prescribed and judicial rates of interest are currently 8%.  The group has discussed reform of this rate in view of the prevailing and long-standing low base rate of interest. | **Prescribed Rate of Interest – Recommendations**  The prescribed rate of interest be reduced to a level that is compensatory rather than punitive. It should be fixed for a period of time and reviewed regularly (suggested every 2-3 years). The rate in force at the start of a bankruptcy should continue throughout the duration of the case irrespective of whether there is a rate change following review in the intervening period as this would avoid complexity and associated costs and be fairer to all those who were impacted.  Although further consultation would be required, the favoured option was an average rate over a fixed period of time + x% (to be agreed). The group considered that eligibility criteria for the application of the prescribed rate of interest should not be changed and not extended to cases where the recall of sequestration was being sought.  There would be merit in aligning the judicial rate of interest with the prescribed rate of interest.  The group consider that the judicial rate of interest should be reduced, preferably to a level consistent with the prescribed rate of interest, if this is possible. However, wider consultation should be carried out to establish the appropriate rate and the impacts on other legislation and stakeholders.  Current legislation should be reviewed, with the default being that post-sequestration interest payable on creditors’ claims be set at the prescribed rate of interest, with individual creditors having to demonstrate good cause for any additional sums they wanted paid under a contractual rate of interest. |
| **Bankruptcy Administrative Procedures**  Some of the administrative arrangements in bankruptcy have been examined to assess areas of increased efficiency and identify processes that are unwieldy. These particularly relate to the functions of the trustee and whether these are necessary or practicable.  These include:   * Setting a Debtor Contribution Order (“DCO”) in a creditor petition bankruptcy * Varying contribution levels * Circulars required on debtor discharge | **Bankruptcy Administrative Procedures - Recommendations**  The current fixed time limit to propose a DCO starting from the date of appointment should be removed. The time limit should be replaced with a requirement for the trustee to submit the DCO proposals as soon as reasonably practicable on receipt of the information or forthwith (or similar wording). If this is not considered acceptable, consideration should be given to extending the current fixed time limit or introducing a simpler procedure for dealing with cases where the current limit cannot be met.  The requirement to circularise creditors giving them the opportunity to make representations over variations in contributions should be reviewed with view to being removed.  Everyone agreed that where a variation is allowed, there should be a facility for it to be backdated, particularly where there are downward variations arising from health grounds or a change in employment status, where it would not be feasible or justifiable to maintain the DCO.  The number of circulars on debtor discharge should be reduced and details of the discharge process be included in the first circular – this would need further consultation and agreement with creditors. There are separate recommendations to change the debtor discharge process and this recommendation will only stand if the current discharge process continues. |