



Home Owner and Debtor Protection (Scotland) Bill

1. The Institute of Chartered Accountants of Scotland (ICAS) is pleased to have the opportunity to submit its views on this Bill to the Local Government and Communities Committee. ICAS welcomes the invitation to supplement this written evidence by providing oral evidence at a meeting of the Committee on 4 November 2009.
2. ICAS authorises and regulates the vast majority of Scotland's Insolvency Practitioners (IPs). IPs deal on a daily basis with debtors, providing free debt advice and acting as trustees. IPs also act as agents for the Accountant in Bankruptcy (AiB), where the agency is the permanent trustee in sequestration.
3. Our interest in this Bill is largely concerned with Part 2 – Sequestrations and Trust Deeds.
4. ICAS was a member of the Debt Action Forum (DAF), set up by the Minister for Community Safety, Fergus Ewing, and had input into some of the changes proposed within this section of the Bill. We welcome the majority of these changes, which will introduce sensible measures to protect debtors in Scotland.
5. That protection has to be balanced with the rights of creditors. The Bill must also ensure that debtors and creditors continue to have a range of choices in debt relief and the safeguards provided by properly qualified and regulated experts.
6. We have concerns about two aspects of Part 2 of the Bill:
 - i. The removal of the family home from protected trust deeds and any other assets subsequently prescribed in regulations. If passed into law, this could have a serious economic impact and deny choice to debtors and creditors.
 - ii. The provisions relating to the certificate for sequestration.

The Intentions of Part 2 of the Bill

7. The Bill has two main aims. First, to provide greater safeguards for the debtor's family home in the insolvency process. Second, to ensure that all debtors can access a debt relief mechanism, including more flexibility for trust deeds. We support both of these intentions in principle.

The Debt Action Forum – Concerns over lack of consultation

8. The Debt Action Forum (DAF) was set up to consider, in light of the economic downturn, early actions that could be taken to help debtors. The group represented a wide range of views from those involved in debt issues. ICAS remains concerned that, despite suggesting the group should include unsecured creditor representation, their views were never fully considered.
9. How to treat the family home was discussed at the DAF. It was recognised as an issue of major importance. As such, the conclusion in the final DAF report of June 2009 stated, "**Members accepted that the whole subject of action against property was complicated and affected a lot of areas. They agreed that this paper raised a number of issues which should only be considered after a full public consultation.**"¹

¹ *Final report of DAF under section 4.3 'Increasing the protections for family homes'*



10. Given this conclusion, we are surprised that a concrete proposal affecting how the family home may be dealt with in a protected trust deed appears in this Bill, without any consultation having taken place. We have had no explanation as to how this proposal was arrived at, and on what evidence it is based.
11. Notwithstanding the fact that there has been no agreement on this proposal at the DAF, it has now become difficult to see the 'big picture' in terms of how debtors are to be treated in relation to their family home. Although this Bill affects how the family home may be treated as an asset in a protected trust deed, it does not consider how it will be dealt with in future in a sequestration. Apparently, this will be discussed in a consultation beginning in November, to be resolved in the Debt and Family Homes Bill. Furthermore, there is an ongoing consultation on the Debt Arrangement Scheme, which also deals with protection of the family home. This means a potential lack of consistency and clarity for all stakeholders with an interest in this legislation.

Option to exclude the family home and other assets from protected trust deeds

12. Protected trust deeds are a voluntary arrangement between a debtor and his creditors. Protection is gained by creditor consent, allowing a trustee to handle the debtor's total assets in order to return money (the dividend) to creditors. When the trust deed is protected, the debtor is free from the risk of legal action from his creditors. It is a commonly used debt relief mechanism in Scotland and has worked effectively for many years.
 13. The Bill changes the *status quo* by allowing the exemption of the family home from protected trust deeds and giving discretion to Scottish Ministers to allow the exemption of other specified assets. We believe there are other technical issues with the definition of trust deeds in the Bill, which we would be happy to address at stage two.
 14. ICAS believes that the proposal seeks to address a problem that does not exist. In a survey which included Scotland's biggest personal insolvency practitioners, there was not a single eviction by a trustee in a trust deed out of a total of 934 protected trust deeds in the past year, where the family home was an asset. There were zero forced sales. The reality is that it is secured lenders who repossess properties and evict owners, as they have first call on the assets. The IP community, legal community and creditor community already work together to ensure that protected trust deed debtors rarely end up in a situation where they find themselves homeless. It is the debtors' decision to grant a trust deed and the implications for the family home are explained in detail to the debtor by an IP before the debtor decides the course of action to pursue.
 15. Against this background, ICAS believes exclusion of the family home and other assets would send out a dangerous message. There is a real risk that where we currently have those who can and those who cannot pay we will be adding a third category of those who don't have to pay. The current proposals could invite debt abuse. It is not difficult to imagine a situation in which an unscrupulous debtor buys an expensive property partly funded by unsecured debt whilst failing to pay his creditors in the full knowledge that the unsecured creditors will not be able to rely on the equity in the house towards settlement of their claims. Although it is up to creditors for a trust deed to become protected we have concerns about possible abuse.
 16. Further, we believe allowing the exemption of the family home and other assets will have the following outcomes:
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- i. The creditor community is unlikely to agree to a debt relief process that excludes the major asset or assets from which a dividend can be paid. Often this asset is the family home. A trust deed that fails to become protected because creditors do not provide consent would result in a trust deed without protection – exposing the debtor to ongoing legal action by creditors and possible sequestration. An option that may then be open would be the certificate for sequestration route proposed in the Bill, however there are few details of how this would operate in practice and the criteria for eligibility.
 - ii. The unsecured creditor community, including HM Revenue & Customs where the individual owes tax or VAT, lending institutions, small tradesmen and personal creditors, expects to be able to recoup debts from the debtor's available assets. The reduced ability to recover debts would have a particularly damaging effect on smaller businesses, which lack the sophisticated credit control and debtor monitoring processes of larger entities. It could jeopardise their cashflow and potentially lead to graver consequences. The proposal could be a major disincentive to consumer lending in Scotland.
 - iii. Institutional lending to smaller businesses would also be influenced by the higher risk premium. This could mean small businesses and others seeking credit in Scotland being treated less favourably by lenders. Secured lenders such as banks will also be conscious of Part 1 of the Bill which will restrict the rights of creditors in repossessions. The aggregate effect may be to tighten lending criteria.
 - iv. The cost to the public purse arising from the reduction in assets available to meet Crown debts should also be considered.
 - v. More debtors would be likely to enter sequestration. In the absence of clarity on the certification route, ICAS believes that this would be the consequence of more debtors having protection for trust deeds refused by creditors. Sequestrations can be a cost to the public purse whereas protected trust deeds contribute to it by providing fees to the AiB, by way of a levy paid by IPs to the agency. A big rise in sequestrations at the expense of the voluntary protected trust deed would fly in the face of one of the main intentions of the recent Bankruptcy and Diligence Act 2007, which sought to reduce the stigma of insolvency.
17. **ICAS believes that the amount of uncertainty and lack of clarity surrounding how the family home should be treated in personal insolvency is too significant an issue to be decided without full and proper public consultation.**
18. **We recommend that the proposal to allow exclusion of the family home and other assets from protected trust deeds should be removed from the Bill and considered alongside other personal insolvency processes such as sequestration.**

Certificate for Sequestration

19. The certification route was conceived to solve one of the main problems the Bill sets out to address, by offering a route to debt relief for those debtors unable to access any form of debt relief.
20. As currently drafted in the Bill, the test a debtor must pass to obtain a certificate for sequestration is one of “practical insolvency” defined as the inability to pay debts as they fall due. Practical insolvency does not, however, necessarily coincide with absolute insolvency, which means that a



certificate for sequestration could be granted and allow a route into sequestration, even for those who have quite substantial assets.

21. This is maybe the policy intention. However, if there are assets involved, the debtor should be allowed a choice as to who should be appointed. Private sector trustees have a great deal of experience in the valuation of assets and dealing with more complex cases and this option may be welcomed by debtors. IPs are highly regulated and trusted by the creditor community to deal with cases involving assets. At present, the Bill sets out that the AiB is the trustee in all certification cases.
22. Certificates for sequestration would be granted by 'authorised persons'. Before dealing with the debtor safeguard issues around authorisation we would again refer to the fact that there is an ongoing consultation on the debt arrangement scheme (DAS), which is considering issues relating to authorised money advisers. We suggest that if money advisers are to be considered as 'authorised persons' for the purposes of granting certificates for sequestration, it makes sense that there is a coherent approach to the two processes.
23. The authorisation process should have guiding principles – debtor protection and preventing abuse. We suggest that regulations should ensure:
 - i. there is provision for the person granting the certificate to have sufficient evidence to be satisfied that it is appropriate to grant it
 - ii. the debtor can have confidence in the authorised person. This means authorised persons must be properly qualified to deal with debtors. They should be regulated and carry professional indemnity insurance.
 - iii. penalties for abuse by unauthorised and unscrupulous advisers; and
 - iv. penalties for abuse by unscrupulous debtors in obtaining a certificate without making a full disclosure.

ICAS solutions

24. ICAS, in a report to the Minister for Community Safety in June 2009, set out simple solutions to the issues that Part 2 of the Bill seeks to address. We strongly recommend that members of the Committee read the report by following this link:

<http://www.icas.org.uk/site/cms/contentviewarticle.asp?article=6300>

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