

July 2023



Bankruptcy and Diligence (Scotland) Bill call for views

Response from ICAS

Scottish Parliament Economy and Fair Work Committee: Bankruptcy and Diligence (Scotland) Bill call for views

About ICAS

- The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants. We represent over 23,000 members working across the UK and internationally. Our members work in the public and not for profit sectors, business and private practice. Approximately 11,000 of our members are based in Scotland and 10,000 in England.
- We are one of the four Recognised Professional Bodies (RPBs) regulating insolvency practitioners (IPs) who can take appointments in the UK. We have an in-depth knowledge and expertise of insolvency law and procedure. We also have experience in other areas of regulation, as a recognised supervisory body (RSB) for statutory audit, and a professional body supervisor (PBS) for anti-money laundering.
- Our charter requires us to primarily act in the public interest. Our responses to consultations and calls for views are therefore intended to place the public interest first. Our charter also requires us to represent our members' views and protect their interests. On the rare occasion that these are at odds with the public interest, it is the public interest that must be paramount.
- We, like our members and the public, are interested in ensuring that any changes to legislation and procedure are made based on a comprehensive review of all options, supported by evidence, with reasonable confidence that the changes will bring benefits to all stakeholders.
- We are pleased to have the opportunity to submit our views in response to the Scottish Parliament's Economy and Fair Work Committee's call for views on the Bankruptcy and Diligence (Scotland) Bill ('the Bill'). We would be happy to discuss any of the matters raised in this response in further detail with the Committee.

General comments

- We are broadly supportive of the changes that will be brought about by the Bill.
- Specifically in relation to the proposed "mental health moratorium", we reaffirm our support for this measure. Recognition of the specific challenges and assistance requirements of those facing mental health issues is a welcome and necessary step in a progressive and modern society. Those who face such challenges are in a vulnerable position, and often at a point when they don't have capacity to engage with their creditors or in court proceedings.
- Answers to specific questions posed in the call for views follow.

21 July 2023

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Specific Questions

Q1. Do you agree that the Scottish Government should take forward legislation in these areas?

A: Yes, we support the Scottish Government taking forward legislation in the areas covered by the Bill.

Q2. What are the key issues that the Scottish Government should consider when developing a mental health moratorium?

A: The current moratorium provisions in Scotland benefit from simplicity of operation. Given the characteristics of those likely to be impacted by the mental health moratorium process, it is important to keep this philosophy in its design.

We support the view that the scope of those who may benefit from such a new process should be wider than those covered under the mental health crisis provisions in England and Wales. However, the difficulties in providing a wider and accessible process alongside appropriate safeguards and protections for other stakeholders, including creditors, is likely to require careful balancing.

It is of note that the Bill and accompanying policy memorandum suggests an application in relation to those who have a “mental illness”. This terminology has changed from the [Stage 2 working group report](#) which recommended such a moratorium, described as a “mental health moratorium”. The accompanying Policy Memorandum states “The overarching policy intention would be to provide protections in addition to those provided through the existing moratorium, with a focus on providing the debtor with breathing space from creditor action in order to focus on treatment for, or recovery from, **serious mental illness.**” [emphasis added]. It is important that the Scottish Government provides clarity at an early stage during the progress of this Bill on their anticipated scope and interpretation. There is currently a lack of clarity and ambiguity over the terminology of mental health, mental illness and serious mental illness and the intended scope of application of the moratorium if the Bill provisions are passed.

It will be crucial to the regulations and to whether the moratorium will achieve its intended outcome, while at the same time offering sufficient safeguards to prevent abuse.

The key issue of difficulty may be less to do with the mechanics of operation and more to do with how mental illness is defined and how that will require to be evidenced for the purpose of access.

Proportionality, and the impact on advisers (most particularly in the already overburdened free advice sector) must also be factored in when considering the scope and development of the moratorium.

In its first full year of operation (2022) fewer than 2% of Breathing Space registrations in England and Wales were mental health crisis moratoriums. In Scotland, for the financial year 2022-23, 3,268 statutory moratoriums on diligence were registered. Making the reasonable assumption that there will be a similar rate of uptake as in England and Wales, even allowing for a slightly wider scope, there are likely to be relatively small numbers utilising the new moratorium.

It should be noted that most debt in personal insolvency situations will come from regulated credit along with local authority debt such as council tax and other governmental debt such as HMRC. We would expect that as a result of the FCA requirements on the regulated credit sectors, including treating customers fairly, that a significant factor in seeking a moratorium would therefore be predicated by local authority and governmental department debt recovery action and would highlight a need for such agencies to work towards identifying vulnerable persons as part of their debt recovery actions which could avoid the need for mental health moratoriums to be sought.

While the moratorium must not be left open to abuse, an overengineered process that potentially dissuades those that need it and makes it overly burdensome for advisers would not strike the correct balance.

On a practical level the case of [Kaye v Lees \[2023\] EWHC 152 \(KB\)](#) provides useful guidance on the necessary conditions for a mental health crisis moratorium in England and Wales. The Scottish Government should be cognisant of the matters considered in that and other court cases and engage

with stakeholders involved in Breathing Space to ensure that lessons can be learned from their experiences.

Engaging with and listening to people directly working in mental health will also be vital to ensure that the entry criteria are correctly scoped and defined, and the evidence requirements fully considered from a practical perspective.

Finally, it is important that the definition of “individuals who have a mental illness” is set out in secondary legislation so they can be more readily amended if issues are identified following the enactment of the moratorium.

Q3. What are the practical implications of the proposed amendments to bankruptcy legislation?

A: We welcome the intention of the amendments contained within clauses 2-5 of the Bill to address identified issues which are minor and technical in nature. These are likely to result in relatively small but important efficiencies in connection with the administration of bankruptcies through clarity of procedures. This may also avoid unnecessary legal procedures and associated costs being incurred because of the existing lack of clarity as well as avoiding costs associated with potential mischievous actions seeking to exploit the lack of clarity and ambiguity in existing legislation.

Q4. Are there any other aspects of the Bankruptcy (Scotland) Act 2016 that you think could benefit from reform?

A: We consider that legislative amendment should be brought forward as a matter of urgency, and prior to the wider stage 3 review, to address the issue of trustees being unable to obtain their discharge where a debtor is unable to be traced or in circumstances where a debtor is non-cooperative long term and avenues to obtain cooperation have been exhausted or impractical to pursue further. It is widely acknowledged that it is undesirable that a trustee must remain in office in perpetuity in such situations, causing practical issues as well as incurring unnecessary costs. We would urge the Scottish Government to bring forward amendments to the Bill at Stage 2 to address this issue and put in place a safe haven scheme for such cases.

We also take the opportunity to, once again, state that we strongly urge the Scottish Government to undertake a full review of how a debtor's heritable property, specifically a family home, should be dealt with across all debt payment and debt relief solutions. This issue is at the heart of all personal insolvency procedures and should be a priority of the Scottish Government. Whilst in recent years this matter has been less of an issue, there is anecdotal evidence that the current cost of living crisis is impacting more homeowners than has recently been the case. As a result, there is an expectation that should there be a material increase in the number of bankruptcies arising from the cost of living crisis, the number of family homes subject to vesting in a bankruptcy and requiring equity to be purchased or the family home to be realised by way of sale could increase substantially.

Aside from those specific points, we advocate that the stage 3 review of debt solutions takes its lead from the review of the personal insolvency framework in England and Wales.

Despite various amendments over the years, the insolvency framework in Scotland has effectively been in place since 1985. Since that time, we have seen a proliferation of consumer credit and markedly changed social attitudes towards debt forgiveness and the stigma that surrounds indebtedness and insolvency.

We consider that a ‘blank page’ review is undertaken to consider whether the current suite of debt solutions in Scotland remain fit for purpose and, if not, what reforms are needed. Specifically, consideration should be given to:

- What the fundamental purpose of the personal insolvency framework should be.
- Are the processes still fit for purpose? Is there still a requirement for both bankruptcy and protected trust deeds, two processes that have become homogenised due to years of legislative tinkering?

That review should also consider matters such as how we, as a society, treat individuals who have a mental illness and have found themselves in problem debt. Notwithstanding our support for the planned mental health moratorium, that moratorium should not preclude this topic for inclusion as part of a wider review.

Societally there must be significant question marks over individuals who have a mental illness (depending on its nature) being placed back into a position of problem debt post-moratorium (with the potential for re-lapse) or finding themselves effectively in a permanent moratorium with no resolution. Consideration of automatic permanent debt-relief would seem appropriate from some individuals in prescribed circumstances.

Finally, we consider that the role of the Accountant in Bankruptcy (AiB) should be reviewed, specifically:

- The conflict of interest in the AiB providing policy and development support for the Scottish government while acting as a provider of insolvency services.
- The appropriateness of the AiB's oversight function. The AiB's supervision of trustees stems from a time prior to the introduction of insolvency practitioner licencing under the Insolvency Act 1986 and is arguably double regulation of the insolvency profession in Scotland.
- How and to what extent the AiB is funded (which will largely be determined by the functions and work carried out by the AiB).

Q5. How will the diligence reform proposals in the Bill impact on creditors and people in debt?

A: Due to the general scope of the work of our members and affiliates, we are not able to significantly comment on the diligence reform proposals.

However, on a general note that ties into this topic (specifically the provision of the debt advice and information package (DAIP)), we are concerned that references to leaflets and the presumption of written material being provided is overly restrictive and does not aid the overall objective of ensuring an individual understands the information they are being provided with.

While we note that the AiB is currently seeking to streamline with DAIP, it is now well understood that individuals have different communication preferences. Written information may not be inclusive where for instance dyslexia or other impairments exist. Such factors need to be given higher priority in formulating proposals and legislative drafting. The use of technology in a variety of different formats and innovative methods of communication should be part of a digital first approach, with other communication channels permissible where appropriate. Such an approach would not only contribute to net zero sustainability targets but also allow innovative developments which might also facilitate checking of understanding should this be desirable rather than just ensuring that information is provided.

Q6. Are there other proposals for diligence reform that should be taken forward in this Bill?

A: See above.

Q7. Do you have any other comments on the Bill or this area of policy?

A: We would be pleased to engage further in discussions on any of the matters set out in this response.



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