RESPONSE TO
CONSULTATION ON
PROPOSALS FOR CHANGES TO PROTECTED TRUST DEEDS
SCOTTISH GOVERNMENT
Introduction

1. The Institute of Chartered Accountants of Scotland (ICAS) is the oldest professional body of accountants and represents over 21,000 members who advise and lead business across the UK and in almost 100 countries across the world. ICAS is a Recognised Professional Body (RPB) which regulates insolvency practitioners (IPs) who can take appointments throughout the UK. We have an in-depth knowledge and expertise of insolvency law and procedure.

2. ICAS’s Charter requires it to primarily act in the public interest, and our responses to consultations 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.

3. ICAS is interested in securing that any changes to legislation and procedure are made based on a comprehensive review of all of the implications and that alleged failings within the process are supported by evidence.

4. ICAS is pleased to have the opportunity to submit its views in response to the Scottish Government's consultation on Proposals for Changes to Protected Trust Deeds. We shall be pleased to discuss in further detail with the Scottish Government any of the matters raised within this response.

Executive summary

5. We agree with the stated intentions of the proposals, namely, to address the concerns raised surrounding Protected Trust Deeds ("PTDs") and to enhance the effectiveness of PTDs through greater transparency and fairness.

6. We do however have concerns that some of the measures will not deliver the intended result. In other circumstances we have concerns that the proposed measures are unnecessary in legislation and that non-legislative measures have not been considered to address matters of concern.

7. ICAS is concerned that, once again, the issues regarding a debtor's heritable property, and particularly a debtor's dwellinghome, remain largely unanswered.

8. ICAS reiterates its call made on numerous occasions previously for the Scottish Government to instigate a full review of how a debtor's heritable property, and in particular equity, should be dealt with across all debt payment and debt relief solutions. This issue is at the heart of all personal insolvency procedures, there should be consistency of treatment and should be a priority of the Scottish Government.

9. We remain concerned that the approach being adopted within 'high equity trust deeds' does not meet with the PTD requirement that all of the assets and property of a debtor are included within the PTD nor does it balance the rights of debtor and creditor. While it has been argued that creditors are accepting of this and therefore no further action should be taken, we would argue that such action fundamentally undermines the credibility of the Scottish insolvency process and is causing significant consumer detriment.

10. It is noted that consultation paper refers to proposed changes to regulations (except for question 5 of Annex B which relates to voting procedure and refers to Section 170(2) of the Bankruptcy (Scotland) Act 2016), these being the Protected Trust Deed (Scotland) Regulations 2013. Whilst noting that the process of reviewing Protected Trust Deeds commenced some time ago and in part considers the effectiveness of changes introduced at that time, the regulations have since been revoked by virtue of the 2016 Act. It would therefore have been more helpful for references throughout the consultation to have referred to the relevant sections of the 2016 Act and for proposed amendments to be in relation to the relevant sections of the 2016 Act.

11. ICAS is also concerned that once again there is a piecemeal approach being taken to legislative change to debt solutions. It is unfortunate that the response to the DAS consultation has not been published sufficiently in advance of this consultation being issued or closing to allow respondents an opportunity to consider the impact of the DAS consultation outcome on their responses to this consultation.

Ensuring PTDs are an appropriate solution for the individual
12. We fully agree that individuals should be directed to appropriate debt solutions. What is an appropriate debt solution will depend upon several factors and on individual circumstances. Over recent years there has been a move through legislative amendments to blur the distinction between the various debt solutions. As a result, it is perhaps rare for there to be a clear case where one solution is the ‘most appropriate solution’. It is important therefore to recognise that there is unlikely to be a right or wrong solution, while recognising that some may have more positive benefits than others. The objective therefore must be to ensure that individuals are in ‘an appropriate debt solution balancing the needs of a debtor and the rights of the creditors’.

13. A clear policy decision requires to be taken on whether the direction of travel for debt solutions in Scotland is to be taken down a route where debtors (and to some extent creditors) are forced into particular solutions or whether there is a choice of solutions available to meet the individual circumstances and preferences of individuals. We would support retaining a choice of solutions being available.

14. We do not agree with the proposals outlined in the consultation to extend prevention of trust deeds being protected where the debtor’s contribution could pay off the debt in full within 60 months. This is because:

- It risks increasing the amount of time individuals are bound into payment plans for up to 25% longer
- It delays the financial rehabilitation of vulnerable individuals
- It risks forcing a greater number of vulnerable individuals into bankruptcy

15. We do not agree that protection should be denied where the debt could be repaid in full over an extended period. We consider that flexibility in availability of debt solutions should be maintained to allow individuals varying circumstances to be considered in determining the debt solutions which may be appropriate to them.

16. We agree that no change should be made to the minimum debt level of £5,000.

Striking the right balance between debtors and creditors

17. The narrative in the consultation paper is far from clear in relation to the matter of the treatment of category one and category two disbursements, with reference variously being made to costs, fees and outlays, all of which are quite distinct.

18. The consultation appears to fundamentally misunderstand the scope of category one and two disbursements which relate only to payments on behalf of an insolvent estate which are met firstly by the office holder before repayment from the insolvent estate. We consider it unlikely that the intention of the proposed change is to be limited to costs which are firstly met by the office holder before repayment from the insolvent estate.

19. We acknowledge that there are wider stakeholder concerns in respect of expenses in personal insolvency procedures but believe that legislation should only be introduced where there is an identified need to do so and where no other appropriate measures could be taken. We are not convinced that this is the case.

20. We would suggest that where there are concerns, they relate primarily to the volume provider market.

21. A range of non-legislative interventions are currently being investigated or are planned to be introduced in the coming months through UK insolvency frameworks. These include changes to SIPs, the insolvency Code of Ethics and the way in which insolvency practitioners in volume providers are monitored. In addition, powers already exist within legislation for the AIB to intervene and carry out an audit and determination of a trustee’s remuneration and outlays.

22. For the reasons outlined above, we do not therefore agree with the proposal to include category one and category two disbursements within the single fixed fee.
23. Whilst not objecting to the introduction of active consent in principle, we do not consider that it will have the impact intended. This is because the protection process is largely controlled by a small number of entities who represent most consumer creditors. Whether a trust deed gains protection or not is largely influenced by whether the trust deed meets their conditions. Where it does not then the creditor representatives will vote against protection. Requiring active consent is unlikely to change the outcome in most cases.

24. We agree that where no creditors vote then the individual seeking a resolution to financial difficulties should not be denied debt relief through creditor indifference to the proposal.

25. We agree with the consultation proposal that no general power should be granted to the AIB to allow refusal of protection. We do not consider that there is a case for state intervention in a contractual arrangement between an individual, their creditors and a trustee.

Confirmation of debt

26. ICAS agrees that the 120-day time limit for claims should be brought in to provide consistency with the process in sequestration.

Detailed response

27. Our response to the key questions contained within Annex B of the consultation paper are set out in Appendix 1.

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1. CONSIDERING IF A PTD IS THE BEST OPTION.

Question 1(a): Do you agree that protection should be refused where the full debt in a trust deed could be repaid in 60 months, through the debtor’s contributions?

Yes ☐ No ☒

Question 1(b): If you answered no to Q1(a), what do you consider an appropriate timescale?

Answer:

We consider that the statements made within paragraph 5 of the consultation document take an overly simplistic view of the criteria used in judgement of whether a particular debt solution provides the best option for an individual.

The consultation document only looks at the comparison between a PTD and DAS, ignoring the further alternative that the debtor would also be eligible for bankruptcy. The consequences of restricting accessibility to a PTD would inevitably result in the decision being narrowed to being between bankruptcy and DAS. This is further expanded upon and discussed in response to Q3.

We do not consider that Table 1 of Annex A to the consultation paper provides an entirely fair comparison. As a result of the Debt Arrangement Scheme (Scotland) Amendment Regulations 2018, a debtor’s income and expenditure must be assessed using the CFT. However, the debtor is not required to pay their full surplus income to their DPP if they choose not to. Considering this, it is impossible to make the 5-year comparison accurately. It should also be emphasised that “full payment” in a DAS can often equate to 90% of the principal debt. With the further changes proposed to DAS fees in the consultation ran by the AiB, which closed on 24 January 2019, this comparison could be rendered further meaningless. It is unfortunate that the response to the DAS consultation has not been published sufficiently in advance of this consultation being issued or closing to allow respondents an opportunity to consider the impact of the DAS consultation outcome on their responses to this consultation.

The sustainability of contributions over a 60-month period is also not given any consideration and some analysis of that would have been beneficial to the consultation.

Fundamentally however, there requires to be a clear policy decision on whether the direction of travel for debt solutions in Scotland is to be taken down a route where debtors (and to some extent creditors) are forced into particular solutions or whether there is a choice of solutions available to meet the individual circumstances and preferences of individuals.

The concept of there being a ‘right solution’ is flawed. This suggest that there can only be a binary decision when in reality taking into account the individual circumstances of each person there is rarely a binary decision of possible solutions. The ‘right solution’ may therefore better described as ‘most appropriate solution balancing the needs of a debtor and the rights of the creditors’.

Safeguards exist in terms of directing people to the correct product. SIP 3.3 makes it clear that an insolvency practitioner should ensure that the advice, information and explanations provided to a debtor about the options available are such that the debtor can make an informed judgement on which process is appropriate to their circumstances.

As the consultation paper states, the current regulations prevent the protection of a trust deed where the proposed contribution would be sufficient to pay off the debt in full in four years or less.

A PTD can be an appropriate solution based on specific individual circumstances. We consider that debtors should continue to have the ability to choose which debt solutions are appropriate to their own circumstances. For example, some individuals may prefer to deal directly with a trustee in a trust deed rather than enter DAS where they would deal with a government agency and payment distributors, particularly where equity in a family home is to be realised. A trust deed may also balance better the rights of creditors in comparison to DAS as they would remain entitled to interest and charges.
We consider that there are significant risks in pursuing a policy of restricted solutions and that it is preferable not to overly restrict entry to debt solutions other than where there are appropriate and practical reasons to do so. For example, it is appropriate for MAP bankruptcy to have restrictive entry conditions as MAP is designed to deal with low level debt relief where there is no possibility of contributions and no assets to be dealt with.

Ignoring at this stage the potential of some debtors to chose bankruptcy where access to a PTD is denied, the effect of the proposed change is to extend the period an individual is bound into a payment plan by 25% or an additional year. Based on Table 1 of Annex A of the consultation document this could affect over 360 individuals per year or 7% of current PTDs.

One of the fundamental drivers behind debt relief being provided within society is to allow individuals to be provided with a ‘second chance’. It is widely recognised and accepted that rehabilitation measures should be swift and no longer than necessary. To force individuals into an unnecessary extended period of debt repayment does not meet these objectives.

While the UK is currently negotiating an exit from the EU, it is perhaps also worth mentioning the anticipated changes that will come through in the EU from a new directive on harmonisation of insolvency and restructuring procedures. The measures within this are anticipated to include a maximum period before discharge from debt of three years and that requirements to make contributions would be based on the debtor’s individual circumstances during the period prior to discharge. While the final terms on which the UK will exit from the EU and the UKs future relationship with the EU remain to be seen, both the EU and UK have indicated that it would be desirable to retain co-operative insolvency frameworks and therefore the likelihood of the UK implementing measures contained within this EU directive would seem to be high. If that were the case, then this would clearly impact on existing PTD provisions. Taking into account other concerns we do not see a strong case for making further changes which impact on the period of a PTD at this stage.

Potential further consequences of the proposed change would be to see a move of individuals from PTDs to unprotected trust deeds as the change would only have a restrictive effect on PTDs. While it is not currently known how many unprotected trust deeds are in existence, the practical consideration of unprotected against protected trust deeds often comes down to the crammed down binding nature of the PTD on all creditors of the individual and consequently the protection against bankruptcy proceedings afforded from creditors who otherwise object to the PTD.

In the current landscape, where the vast majority of PTDs are in respect of consumer debt and the FCA requirements around treating customers fairly and commercial decision making around the prospects of recovery from bankruptcy proceedings, the risks associated with an non-acceding creditor pursuing bankruptcy when there is a trust deed in place under the control of an authorised insolvency practitioner is now likely to be considered remote. Consequently, the advantages the introduction of protected trust deeds were designed to provide are diminished.

2. PAYMENT OF DEBTOR’S CONTRIBUTION - REGULATION 8

Question 2(a): Do you agree that a trust deed should not be eligible for protection where the value of contributions over its extended period is equal to or greater than the level of debt present when it was granted?

(Protected trust deeds are typically extended to allow payments to be made in lieu of property equity.)

Yes ☐ No ☒

Question 2(b): If you answered no to Q2(a), why not?

Answer:

We would refer to comments made in respect of Q1 above which apply equally to extended periods.
3. MINIMUM DEBT LEVEL – REGULATION 4

Question 3(a): Do you think that the minimum debt level allowed in a PTD should be increased from £5000?

Yes ☐ No ☒

ICAS considers that it would be inappropriate to increase the minimum debt level in view of feedback from the previous consultations that an increase would potentially force vulnerable individuals into bankruptcy.

Based on Table 1 in Annex A to the consultation document, this measure could affect up to 27% of debtors currently entering a PTD, resulting in nearly 1,500 additional bankruptcies per year.

Please also refer to comments made in relation to Q1 concerning the policy approach to restricting access to debt solutions and existing safeguards that are in place to ensure that debtors access appropriate debt solutions.

Question 3(b): If you answered yes to Q3(a) at what level would you set the minimum debt level at?

£7,500 ☐ £8,000 ☐ £10,000 ☐ Other ☐

(please state your preferred level)

Question 3(c): If you answered other to Q3(b) what do you think the minimum debt level should be?

Answer___________________________________________________________

4. REMUNERATION PAYABLE TO TRUSTEE UNDER PROTECTED TRUST DEED – REGULATION 23

Question 4(a): Do you agree that category one and two disbursements should be included in the fixed fee?

Yes ☐ No ☒

Question 4(b): If you answered no to Question 4(a), why not?

Answer:
The consultation appears to fundamentally misunderstand the scope of category one and two disbursements.

The definition of category one and two disbursements is found only in SIP9, a statement of insolvency practice issued by Recognised Professional Bodies who authorise and supervise insolvency practitioners. SIPs set principles and key compliance standards with which insolvency practitioners are required to adhere to.

The relevant provisions of SIP 9 (Scotland) are set out below:

“18. Costs met by and reimbursed to an office holder in connection with an insolvency appointment should be appropriate and reasonable. Such costs will fall into two categories:

a) Category 1 disbursements: These are costs where there is specific expenditure directly referable both to the appointment in question and a payment to an independent third party. These may include, for example, advertising, room hire, storage, postage, telephone charges, travel expenses, and equivalent costs reimbursed to the office holder or his or her staff."
b) Category 2 disbursements: These are costs that are directly referable to the appointment in question but not to a payment to an independent third party. They may include shared or allocated costs that can be allocated to the appointment on a proper and reasonable basis, for example, business mileage.

19. Category 1 disbursements can be drawn without prior approval, although an office holder should be prepared to disclose information about them in the same way as any other expenses.

20. Category 2 disbursements may be drawn if they have been approved in the same manner as an office holder’s remuneration. When seeking approval, an office holder should explain, for each category of expense, the basis on which the charge is being made."

As can be seen from the above, category one and two disbursements relate only to costs which have been met firstly by the office holder and are then repaid to the office holder from the insolvency estate.

It appears to be a common misconception that category one and category two refers to all expenses and is simply a way to distinguish between payments made to independent third parties and payments made to the office holder, their firm or a connected party. The correct distinction that category one and category two relates only to repayments to the office holder of costs firstly met by them is confirmed in paragraph 69 of the judgment of Judge Pelling in the case of Varden Nuttall Ltd v Nuttall & Anor [2018] EWHC 3868 (Ch).

We consider it unlikely that the intention of the proposed change is to be limited to costs which are firstly met by the office holder before repayment from the insolvent estate.

We acknowledge that there are wider stakeholder concerns in respect of expenses in personal insolvency procedures. The Insolvency Service in their Report on the monitoring and regulation of insolvency practitioners published in September 2018 raise similar concerns (pages 13-16). While the Insolvency Service report covers a themed review of volume IVA providers, the PTD provider market is comparable. In 2017-18 two firms accepted trustee appointments in 54% of PTDs granted. Those two firms also accounted for 45% of IVA appointments in 2018.

There is little evidence however that the issues identified permeate below the volume providers. It is widely acknowledged that there is a two-tier personal insolvency market. One tier is operated by volume providers, typically operated on a highly commercialised basis in a very corporate environment and controlled by persons who are not typically insolvency practitioners or chartered accountants. They typically obtain their appointments through large advertising campaigns and third party ‘lead generators’. A second tier is operated under a more traditional model where the appointments are held by insolvency practitioners within entities which are controlled by insolvency practitioners and chartered accountants.

We firmly believe that legislation should only be introduced where there is an identified need to do so and where no other appropriate measures could be taken. We are not convinced that this is the case.

Following on from the Insolvency Service report, there are no plans in place at present to introduce legislative measures in relation to IVAs in England and Wales. Instead the Insolvency Service and the Recognised Professional Bodies are working collaboratively to identify effective ways of addressing the issues. Already, through the Joint Insolvency Committee, steps are being undertaken to identify whether there is a need to amend the provisions of SIP 9 or other SIPs such as SIPs 3.1 and 3.3 which relate specifically to IVAs and PTDs. Changes are being introduced to a revised insolvency Code of Ethics, due to come into effect on 1 January 2020, which address matters connected to personal and business relationships, the IP as an employee and the use of services other than provided by the IP. The Insolvency Service are also undertaking a review of the regulation of IPs which will also consider whether there is a need to regulate the insolvency firms as well as the insolvency practitioners. The Insolvency Practitioners Association, who monitor the vast majority of volume providers, have also announced specific measures to strengthen their monitoring regime of volume providers.

Notwithstanding the measures outlined above, it is already open to the AiB, in terms of S183(8), to audit the trustee’s accounts and fix the outlays of the trustee in the administration of the trust. There is therefore a mechanism to deal with any concerns regarding inappropriate charging or inappropriate expenses being incurred.
Given that the perceived issues extend to a relatively small number of PTD providers, albeit affecting a significant percentage of cases, we consider that a more proportionate response at this time would be to make more use of existing legislative provisions and keep under review the effectiveness of non-legislative measures which are being undertaken. Should these measures not prove effectively only then should further legislative provision be considered.

Should any change be taken forward in this area at this time then this would require to be drafted in a manner which covers the expenses (outlays) of the insolvency process, irrespective of whether they were paid firstly by the office holder or his firm or paid directly out of the funds held in the insolvent estate. That however may cause further complications in terms of appropriately considering the differing types of expenses such as costs of asset realisations, statutory fees, remuneration and other expenses.

If it is ultimately decided to include all fees and outlays in the fixed fee, there needs to be consideration of the impact on the various sections of Part 14 of the 2016 Act generally, with the various references to remuneration, fees and outlays. The whole Part of the Act should read cohesively and there should be no unintended consequences as a result of the change.

5. VOTING PROCEDURE IN PTD SECTION 170 (2) OF THE BANKRUPTCY (SCOTLAND) ACT 2016

Question 5(a): Should the voting system for PTDs be restructured where a trust deed would only be protected if out of the creditors who have voted those who own 75% of the value of debt have actively accepted the terms of the trust deed?

Yes ☐ No ☒

Question 5(b): If you answered no to Question 5(a), what should the terms be?

Answer:

Whilst not objecting to the introduction of active consent in principle, we do not consider that it will have the impact intended.

PTD protection is generally controlled by a small number of entities who represent a significant number of major creditors’ interests. Currently, if the PTD does not meet their criteria then they will object to the PTD becoming protected. These representatives will participate in the PTD process as they do now and will continue to drive whether protection status is achieved in most cases by reference to their own criteria. It is not considered that smaller creditors, such as Credit Unions, will benefit greatly from this change in terms of having their voices heard and making any significant impact on whether a PTD becomes protected or not.

Question 5(c): Do you believe that AiB should be given general powers to refuse the protection of a trust deed?

Yes ☐ No ☒

The consultation document recognises that the trust deed remains in essence a private arrangement between a debtor, their creditors and the trustee. Interference in such an arrangement by the state therefore must be restricted to essential situations where there is the potential for widespread public harm or where there is some other justifiable reason for interference (for example where it become apparent that the trust deed was based on false information or statements).

We do not believe that there is a case for general powers to be given to the AiB to refuse the protection of a trust deed, regardless of whether the voting procedure is changed.

Any such powers would require to be more specific in their nature. It is not appropriate to have a 'catch all' which would effectively confer significant power on the AiB to affect the PTD process
We therefore agree with the proposal within the consultation document that no amendment to legislation should be made in respect of the AiB’s powers to refuse the protection of a trust deed.

**Question 5(d): If you answered yes to Question 5(c) should these general powers to refuse the protection of a trust deed only be introduced if the creditor voting procedure does not change?**

Yes ☐ No ☑

**Question 5(e): If no creditors respond to the trust deed proposal do you agree that the trust deed should become automatically protected?**

Yes ☑ No ☐

While automatic protection where the creditors do not respond seems at odds with the proposal for active consent, we do consider that financially distressed and vulnerable individuals should not be denied access to appropriate debt relief due simply to creditors being indifferent to the proposed trust deed.

Please use the box below for any other comments you may have, or anything you feel is not covered in the consultation questions.

**FURTHER COMMENTS**

ICAS is concerned that, once again, the issues regarding a debtor’s heritable property, and particularly a debtor's dwellinghome, remain largely unanswered. Whilst noting the steps taken by the Accountant in Bankruptcy in issuing two ‘Dear IP’ letters, ICAS reiterates its call made on numerous occasions previously for the Scottish Government to instigate a full review of how a debtor's heritable property, and in particular equity, should be dealt with across all debt payment and debt relief solutions. This issue is at the heart of all personal insolvency procedures; there should be consistency of treatment and should be a priority of the Scottish Government.

The consultation paper suggests that the issues of the Dear IP letters “is starting to bring about a change in behaviour”. However, this claim appears to be purely anecdotal with no evidence provided in support.

We remain concerned that the approach being adopted within some trust deeds to realise a very small proportion of equity does not meet with the PTD requirement that all of the assets and property of a debtor are included within the PTD nor does the acceptance of such amounts balance the rights of debtor and creditor. While it has been argued that creditors are accepting of this and therefore no further action should be taken, we would argue that such action fundamentally undermines the credibility of the Scottish insolvency process and is causing significant consumer detriment. It is arguable that this area is impacting more on whether debtors are accessing the most appropriate debt solution than the other areas being consulted on with a view to ensuring debtors access the most appropriate debt solution.
Scottish Government Proposals for Changes to Protected Trust Deeds

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Full name or organisation’s name

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