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SPICe Briefing
Bankruptcy (Scotland) Bill

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This briefing looks at the Bankruptcy (Scotland) Bill. The Bill is a Consolidation Bill and therefore makes no changes to the substantive law on the subject. Thus, this briefing looks only at relevant background information, including:

- the procedure for considering a Consolidation Bill,
- the existing bankruptcy process,
- other statutory options for dealing with debt, and
- recent legislative reform in this area.

The Scottish Parliament
Pàrlamaid na h-Alba

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EXECUTIVE SUMMARY

Introduction

The Bankruptcy (Scotland) Bill is a Consolidation Bill. It was introduced by the Scottish Government on 30 October 2015.

Consolidation Bills

Consolidation Bills bring together existing legislation in a more logical and coherent form, so that the law is easier to understand. They do not change the substantive law on the subject. It is, however, possible for Consolidation Bills to take forward Scottish Law Commission recommendations which make minor changes to the existing law.

Consolidation Bills are considered under a special Scottish Parliament procedure which differs significantly from the usual way the Scottish Parliament scrutinises bills. In particular, they are considered by a specially created committee, or by the Delegated Powers and Law Reform Committee.

Amendments are only admissible if they do not cause the bill to cease to be a Consolidation Bill. This means that amendments which seek to change the substantive law are not permissible.

Bankruptcy

Background

When a person or entity becomes bankrupt, their estate is administered by a trustee for the benefit of their creditors. Their "estate" is all their non-essential assets, including land and buildings (and a family home). The trustee is usually a Scottish Government agency called the Accountant in Bankruptcy. It can also be an insolvency practitioner in private practice.

Individuals (including the estates of deceased individuals) can become bankrupt. Partnerships, trusts, unincorporated associations and certain "bodies corporate" can also become bankrupt. The insolvency of companies and limited liability partnerships is dealt with under a different regime which is mainly reserved to Westminster.

Accountant in Bankruptcy

The current Accountant in Bankruptcy is Richard Dennis. He is an officer of the court with responsibility for supervising the bankruptcy process. He also heads up an executive agency of the Scottish Government with various administrative responsibilities in relation to bankruptcy.

The bankruptcy process

When a debtor becomes bankrupt, ownership of their non-essential assets passes to the trustee. The trustee will usually sell these, but he or she can continue the debtor's business if this is considered to be a better option for creditors.

A debtor will also be expected to make a contribution to the bankruptcy from any income they have. The process for assessing whether an individual debtor has any surplus income to pay to creditors is standardised. It uses a system called the "Common Financial Tool".

In order to become bankrupt, a debtor must be insolvent. This can be demonstrated by meeting the legal definition of “apparent insolvency”. Individual debtors can also use a “certificate for sequestration” issued by a money adviser.

A debtor can apply to the Accountant in Bankruptcy for their own bankruptcy. They can also be forced into bankruptcy by a creditor in certain circumstances. The creditor must petition for bankruptcy in court.

There are two bankruptcy processes which can apply to individual debtors. The “full administration” process is the standard process. However, a “Minimal Asset Process” (MAP) is available for low income debtors with few assets. Other entities applying for their own bankruptcy must usually have the agreement of a creditor. Partnerships can apply for their own bankruptcy without creditor agreement.

A trustee is responsible for administering the debtor’s estate on behalf of creditors. This will usually involve:

- taking ownership of the debtor’s non-essential assets and deciding what to do with them,
- deciding on claims from creditors for payment,
- making periodical payments to creditors out of money raised from the debtor’s estate.

The Accountant in Bankruptcy has a general role in supervising a trustee. Trustees can also take advice and instructions from creditors. Trustees need permission from the sheriff to undertake certain actions, and most decisions can be appealed to the sheriff.

Debtors will usually be discharged from bankruptcy after one year. However, the Accountant in Bankruptcy can extend this period if the debtor has failed to co-operate during the bankruptcy process. After discharge, a debtor is no longer restricted by their status as a bankrupt. Most debts will also be written off. However, they will be expected to continue to make payments from income – and to declare any assets they acquire – for a further three years.

Other statutory debt options

There are two other options laid down in legislation for debtors who cannot pay their debts. A protected trust deed is a voluntary arrangement between a debtor and their creditors. It is administered in a very similar manner to bankruptcy. It is an insolvency procedure and, at the end of the process, most debts are written off. The Debt Arrangement Scheme allows debtors to pay their debts in full over a longer period.

Debtors may also negotiate informal repayment arrangements with their creditors. However, creditors are not bound to agree to – or stick to – proposals. This makes them an unstable option.

Recent legislative reform

The Bankruptcy (Scotland) Act 1985 has been heavily amended, which is the main reason for pursing consolidation. Amending legislation has included:

- the Bankruptcy (Scotland) Act 1993
- the Bankruptcy and Diligence etc. (Scotland) Act 2007
- the Home Owner and Debtor Protection (Scotland) Act 2010, and
- the Bankruptcy and Debt Advice (Scotland) Act 2014.

INTRODUCTION

The Bankruptcy (Scotland) Bill ("the Bill") is a Consolidation Bill. It was introduced in the Scottish Parliament by the Scottish Government on 30 October 2015. The Scottish Parliament's procedure for dealing with Consolidation Bills is discussed below.

The Bankruptcy (Scotland) Bill is a pure Consolidation Bill, meaning that it is not intended to make even minor changes to the existing law. Thus, instead of discussing the proposals in the Bill, this briefing considers only the background to the Bill, including the current law in relation to bankruptcy.

THE CONSOLIDATION PROCESS

BACKGROUND

A Consolidation Bill is a very specific form of legislation. It has its own procedure for consideration in the Scottish Parliament's Standing Orders. Under rule 9.18.1, a Consolidation Bill is:

> "… a Bill the purpose of which is the consolidation of enactments, whether or not with amendments to those enactments to give effect to recommendations of the Scottish Law Commission or of the Scottish Law Commission and the Law Commission jointly …"

The Stair Memorial Encyclopaedia (an authoritative source for Scots law) gives a more detailed definition of the purpose of consolidation legislation. It states (Volume 22, paragraph 698):

> "A consolidation Act is an enactment which, without making any changes in the law, brings together in one Act the Statutory provisions relating to a particular topic and repeals the former enactments. The object of the Act is to tidy up the statute book and make the statutory provisions concerned more accessible to the user."

The Scottish Parliament's Guidance on Public Bills (2007) gives further explanation of the scope of a Consolidation Bill. It states (paragraph 3.36):

> "Where the statutory basis of the law in a particular area is scattered among a wide range of Acts, or where those Acts have been heavily amended, it may be appropriate to introduce a single Consolidation Bill to re-enact the existing provisions in a more logical and coherent form. Such Bills are usually prepared by the Executive in conjunction with the Scottish Law Commission. A Consolidation Bill may make various minor amendments to the law (particularly to give effect to Scottish Law Commission recommendations) as well as simply re-stating it, but may not contain substantial new provisions, nor make substantial changes to the existing law."

Broadly speaking, a Consolidation Bill should update the language and structure of existing legislation so that it is easier to understand. Often, it will also involve bringing several enactments together in one new piece of legislation.

The Bankruptcy (Scotland) Act 1985 ("the 1985 Act") has been heavily amended. The Scottish Law Commission stated (2013, paragraph 1.1) that the 1985 Act:

> "has been so heavily amended, on so many occasions, that it has lost coherence and rational structure. Many of its provisions (whether sections, subsections or paragraphs) are inordinately long; and numbering has become complex and unwieldy."

The consolidation process is intended to deal with these issues. Provisions around Protected Trust Deeds (discussed below), which currently appear in subordinate legislation, would also be consolidated into the Bill.

SCOTTISH PARLIAMENTARY PROCEDURE

As noted above, Consolidation Bills have their own specific parliamentary procedure. This is described in Rule 9.18 of the Scottish Parliament's Standing Orders.

A Consolidation Bill does not require to be accompanied by a Financial Memorandum, Explanatory Notes or a Policy Memorandum. However, it must instead be accompanied by tables of derivations and destinations. A table of derivations shows which currently enacted legislation a Consolidation Bill's provisions come from. A table of destinations shows where existing legislative provisions will appear in the Consolidation Bill.

During Stage 1 consideration of a Consolidation Bill, the committee does not report on the general principles of the bill. Instead, it reports on whether a bill should proceed as a Consolidation Bill. The whole Scottish Parliament will then be invited to vote on that issue by way of a motion tabled by the member in charge of the bill. There will not normally be a debate.

If the Scottish Parliament agrees the Stage 1 motion, the Consolidation Bill can progress to Stage 2. As with other bills, an amendment to a Consolidation Bill will only be admissible if it is relevant to the bill or to the provisions it would amend.

In addition, an amendment will not be admissible if it "would cause the Bill to cease to be a Consolidation Bill" (Scottish Parliament Standing Orders, Rule 9.18.8). This means that amendments which would change the substantive law – rather than the way that law is expressed in the Consolidation Bill – would not be admissible.

In the case of the Bankruptcy (Scotland) Bill, the Scottish Law Commission's recommendations on the topic have already been integrated into the substantive law through the Bankruptcy and Debt Advice (Scotland) Act 2014.

At Stage 3, there will usually be no debate on the question as to whether the bill be passed.

Normally, a Consolidation Bill is dealt with by a Consolidation Committee. That is a committee established specifically to consider the bill under the procedure laid out in Rule 9.18. However, a recent rule change allows the Parliamentary Bureau to propose that a Consolidation Bill is referred to the Delegated Powers and Law Reform Committee instead. A motion agreeing this change was passed by the Scottish Parliament (2015, col 77) on 27 October 2015.

It is expected that the Bankruptcy (Scotland) Bill will be considered by the Delegated Powers and Law Reform Committee.

THE SCOTTISH LAW COMMISSION REPORT

The Scottish Law Commission published a Report on the Consolidation of Bankruptcy Legislation in Scotland in 2013, including a draft bill. The report made a number of recommendations designed to improve the law in this area, as well as consolidating existing statutory provisions.

In 2013, after the Scottish Law Commission report was published, the Scottish Government brought forward the Bankruptcy and Debt Advice (Scotland) Bill. This became the Bankruptcy and Debt Advice (Scotland) Act 2014. It made further changes to bankruptcy legislation, rendering the Scottish Law Commission's draft bill redundant.

However, the Bankruptcy and Debt Advice (Scotland) Act 2014 also took forward the recommendations made in the Scottish Law Commission's report on changing the existing law. Thus, the Bankruptcy (Scotland) Act 1985 was amended to reflect the vast majority of the Scottish Law Commission's recommendations.

There are several outstanding Scottish Law Commission recommendations. Some of these are no longer relevant in the context of other reforms to the law.

Two (recommendations 32 and 37) are outwith the legislative competence of the Scottish Parliament. They will be taken forward at Westminster via a section 104 order. This is a procedure under the Scotland Act 1998 which allows modifications to be made to reserved law as a consequence of legislation passed by the Scottish Parliament. Section 104 orders are considered by the UK Parliament.

One recommendation is to consolidate Protected Trust Deed regulations into an Act of the Scottish Parliament (recommendation 38). This is being taken forward in the Bill.

As a result of this, the Bankruptcy (Scotland) Bill can proceed as a pure Consolidation Bill. It is not intended that it will make even minor changes to the existing law.

BANKRUPTCY – AN INTRODUCTION

BACKGROUND

At common law, a debtor in Scotland could escape imprisonment for their debts by surrendering all their property to their creditors. The common law is the traditional law and the law as developed by judges in individual decisions.

The modern law of bankruptcy has its roots in this legal principle. It is set out in the 1985 Act as heavily amended.

Bankruptcy is one of several statutory methods of dealing with debts. The other options, and their relationships to bankruptcy, are discussed in the section following this.

The bankruptcy process set out in the 1985 Act can be applied to individuals, including the estates of deceased individuals. Personal business debts are included in the bankruptcy process. However, the debts of a business association (such as a company or partnership) are treated differently.

The 1985 Act process also applies to trusts, partnerships and unincorporated bodies (such as many clubs and associations). In addition, "bodies corporate" can enter bankruptcy, although not companies or bodies which are prevented by statute from being made bankrupt.

Different insolvency procedures apply to companies and limited liability partnerships. These are mainly reserved to the Westminster Parliament.

THE ROLE OF THE ACCOUNTANT IN BANKRUPTCY

The office of Accountant in Bankruptcy was created by the Bankruptcy (Scotland) Act 1856. The Accountant in Bankruptcy's duty was to supervise all bankruptcy proceedings.

The modern Accountant in Bankruptcy ("the Accountant") is an officer of the court, although the office also has executive functions conferred on it by Scottish Ministers. The current Accountant is Dr Richard Dennis. The Accountant appoints staff and agents to carry out work on his behalf.

The Accountant currently has the following duties under the 1985 Act:

- the supervision of trustees and commissioners in bankruptcy – and trustees in protected trust deeds – in carrying out their legal functions,
- acting as trustee in certain bankruptcies,
- auditing the accounts of trustees (in both bankruptcy and protected trust deeds) and fixing their fees and outlays where requested to do so,
- the determination of debtor applications for bankruptcy,
- maintenance of the Register of Insolvencies, and
- the provision of an annual report to the Court of Session and Scottish Ministers.

Where the Accountant has reason to believe that a trustee is not performing their legal duties, he must report the matter to the sheriff (who can take steps to censure or remove the trustee from office). If he suspects a criminal offence has been committed by a trustee, debtor or third party, he must report the matter to the Lord Advocate.

Under the Debt Arrangement and Attachment (Scotland) Act 2002, the Accountant is responsible for the administration of the Debt Arrangement Scheme (discussed below), including the approval of debt payment programmes.

ADMINISTERING THE BANKRUPT ESTATE

Treatment of assets

When a debtor becomes bankrupt, their "estate" (any non-essential assets, including land and buildings) is administered by a trustee for the benefit of their creditors. It is common for the trustee to be the Accountant in Bankruptcy. However, it can also be an insolvency practitioner in private practice.

In most cases, a trustee will seek to sell a debtor's assets to raise money to pay back debts. This will usually include any family home. However, it is possible for a trustee to continue a debtor's business activities if this is considered to be more beneficial for creditors.

Any assets a debtor acquires within the four years after they become bankrupt will also automatically become the property of the trustee. Examples might be a house or money inherited by the debtor.

Treatment of income

A trustee will also seek a contribution from an individual debtor's income. Those who have a very low income or are reliant on certain social security benefits are not required to make a contribution. However, those on higher incomes may be expected to make a contribution.

The process for assessing how much of a contribution from income an individual debtor should make is standardised. A system called the Common Financial Statement (available under licence from the Money Advice Trust) is used. This is referred to in legislation as the "Common Financial Tool". It takes figures based on average spending on various budget lines by low income families to set thresholds for reasonable expenditure.

When calculating what contribution a debtor can afford, any expenditure up to the thresholds is discounted. Provision is also made for situations where a debtor's unusual circumstances require expenditure above the threshold.

The Accountant sets the amount a debtor must pay from income in a "debtor contribution order". Where a debtor has a poor payment record, the trustee may require a third party to make payments directly to them. For example, a trustee can require an employer to deduct the required contribution from the debtor's wages.

The requirement to make contributions from income will usually last for four years (although this may be extended).

Costs of administering a bankruptcy

The costs of administering a bankruptcy are met from the debtor's estate and, where there is insufficient money, by the trustee. This is the reason why most individual bankruptcies are administered by the Accountant and his staff.

Insolvency practitioners in private practice are unlikely to be willing to take on the role of trustee unless they can be sure that there are sufficient funds in the estate to meet their fees and costs. Thus, in most individual bankruptcies, the Accountant is the trustee and any shortfall in administration costs is met by the public purse.

Accountant in Bankruptcy staff contract with several firms of insolvency practitioners to carry out bankruptcy administration on behalf of the Accountant. However, the trustee is still the Accountant in Bankruptcy.

ROUTES INTO BANKRUPTCY

There are a number of ways for someone to become bankrupt. People can apply for their own bankruptcy.

Debtors who have no prospect of paying their debts in the medium to long-term may want to become bankrupt. Almost all debts are written off at the end of the bankruptcy process, giving debtors a fresh financial start.

Creditors may phone and write to debtors on a regular basis demanding payment of their debts. This can make it difficult to keep on top of finances, especially for low income debtors. Once a debtor enters bankruptcy, creditor contact with the debtor should stop. The trustee will deal with their claims. In addition, creditors are prevented from taking court action to enforce their debts.

It is also possible for a creditor to petition the court to force someone into bankruptcy. This may be very stressful for the debtor concerned. Over the past year, creditor petitions have made up around 20% of all bankruptcies (Accountant in Bankruptcy 2015).

Often debtors do not want to be made bankrupt because they think that, with just a little more time, they will be able to get on top of their financial situation. Sometimes even debtors who cannot pay their debts in the medium to long-term may not want to become bankrupt. This may be because of the stigma still associated with bankruptcy. It can also be because they do not want to lose the family home.

Before a debtor can apply for their own bankruptcy, they must demonstrate that they are insolvent (in other words, unable to pay their debts). This can be done by demonstrating "apparent insolvency" or by obtaining a "certificate for sequestration". A debtor who has granted a trust deed (see below) which has not become protected can also apply for their own bankruptcy.

Apparent insolvency

For a debtor who is an individual, apparent insolvency is usually demonstrated when they fail to pay a debt after an official court demand to do so.

Demonstrating apparent insolvency has traditionally been a barrier to individuals applying for their own bankruptcy. Creditors don't generally take court action against debtors with no obvious assets (although they may threaten to). This is because they run the risk of being unable to recover their costs if they cannot take enforcement action against the debtor. Thus, such debtors have no way of demonstrating apparent insolvency.

The "Low Income Low Assets" (LILA) route into bankruptcy was introduced by the Bankruptcy and Diligence etc. (Scotland) Act 2007. It is discussed in more detail below. It was not necessary to demonstrate apparent insolvency in order to become bankrupt under this scheme.

Partnerships, trusts and other bodies for which bankruptcy under the 1985 Act is possible can also demonstrate apparent insolvency. This is done by giving written notice to creditors that they can no longer pay their debts in the normal course of business.

Certificate for sequestration

An individual debtor can also enter bankruptcy if they have a certificate for sequestration issued by an approved money adviser. A money adviser can issue such a certificate where the debtor can demonstrate that they are unable to pay their debts as they become due.

The certificate for sequestration was introduced by the Home Owner and Debtor Protection (Scotland) Act 2010. Its purpose was to make it possible for those who could not demonstrate apparent insolvency – and could not access the LILA route into bankruptcy because, for example, they owned a house – to become bankrupt.

Bankruptcy of an individual

The main routes into bankruptcy for an individual are described below.

Full administration bankruptcy

This is the traditional form of bankruptcy. An individual can apply for their own bankruptcy via full administration if they owe £3,000 or more.

The other conditions which must be met are:

- The debtor must be habitually resident in Scotland.
- They must be insolvent.
- They must have received money advice from an approved adviser.
- They must pay the £200 application fee.
- They must not have been made bankrupt in Scotland in the past five years.
- The must have signed a "statement of undertakings" outlining their obligations to the trustee.

A creditor can petition the courts to make a debtor bankrupt if the creditor is owed £3,000 or more[1]. The debtor must be apparently insolvent. Individual debtors must be given a “debt advice and information package”. This leaflet gives practical information about dealing with debt.

A trustee in a trust deed (discussed below) can also petition for a debtor’s bankruptcy. This can happen where the debtor has failed to co-operate with the trustee, or where bankruptcy would be in the best interests of creditors.

Minimal Asset Process

The Bankruptcy and Debt Advice (Scotland) Act 2014 introduced a new route into bankruptcy for individuals with little income and few assets. This replaced the LILA route into bankruptcy created by the Bankruptcy and Diligence etc. (Scotland) Act 2007.

The Minimal Asset Process (MAP) is available to individual debtors who meet the following requirements:

- They must owe at least £1,500 but not more than £17,000.
- They must be habitually resident in Scotland.
- They must have received money advice from an approved adviser.
- They must have a certificate for sequestration.
- They must be assessed has having to make no contribution from income using the Common Financial Tool, or they must have been receiving certain social security benefits for at least six months.
- They must not own land or buildings.
- Their non-essential assets must be worth £2,000 or less (with no individual asset worth more than £1,000).
- They must pay the £90 application fee.
- They must not have been made bankrupt in the past five years.
- They must not have been made bankrupt under the Minimal Asset Process in the past 10 years.

The trustee in a MAP bankruptcy will always be the Accountant in Bankruptcy. He can follow a less onerous administrative process to deal with the debtor’s estate. This enables the Accountant in Bankruptcy to charge a lower fee for this type of bankruptcy.

A debtor who is discovered not to meet the qualifying criteria for a MAP bankruptcy can be transferred into the full administration process.

Bankruptcy of partnerships, trusts etc.

Entities such as partnerships and trusts may also apply for their own bankruptcy, or be forced into bankruptcy by a creditor, where they are apparently insolvent. In the case of trusts and other entities, they must have the agreement of a creditor (or creditors) who is owed at least £3,000 to apply for their own bankruptcy.

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[1] Two or more creditors can jointly petition for bankruptcy if they are together owed £3,000 or more.

All entities can be made bankrupt where a creditor (or creditors) who is owed £3,000 or more petitions the courts.

Partnerships are able to apply for bankruptcy without the agreement of a creditor. The trustee in a trust deed (see below) is also able to apply for a partnership's bankruptcy.

WHAT HAPPENS AFTER A PERSON OR ENTITY IS MADE BANKRUPT

Overview

As noted above, a trustee is responsible for administering the debtor's estate for the benefit of creditors. This will usually require the trustee to:

- take ownership of the debtor's non-essential assets and decide what to do with them,
- decide on claims from creditors for payments, and
- make periodical payments to creditors out of money raised from the debtor's estate.

Taking ownership of the debtor's assets

The debtor's estate may be simple to administer. For example, there may be no non-essential assets. However, an estate can also be very complex – containing, for example, foreign property, investments and contractual business rights. Given the wide range of scenarios a trustee might find themselves in, it can take time to track down – and then decide what to do with – a debtor's assets.

The trustee will make up an inventory and valuation of the debtor's estate.

Deciding on claims from creditors

The trustee must also invite claims from creditors. He or she is entitled to see proof that a debt is genuine. The trustee will make the initial decision about whether to accept a creditor's claim. Such a decision can have a significant impact not only on the creditor, but on the debtor and other creditors in the bankruptcy. All are entitled to challenge the trustee's decision in the sheriff court.

Making payments to creditors

The trustee is also responsible for making periodical payments to creditors, based on the money he or she has been able to raise from the debtor's estate. It is usual for payments to be made every 12 months, but this period can be varied.

There is a hierarchy to the order in which payments to creditors are made. This means that some debts may be paid in full where as others may not be paid at all.

The remuneration and outlays of the trustee are the first expense which is paid out of the debtor's estate. Any "deathbed" and funeral expenses of the debtor are next, rating equally with the expenses of an executor of a deceased debtor's estate. Then the expenses of the petitioning creditor (or creditors) can be met. Together these are known as "prior debts".

Only once prior debts have been met in full will the trustee be able to distribute funds to the creditors. Certain debts are "preferred" and are paid in full first. These include certain pension contributions and the wages of employees (up to a £800 cap).

Historically, a number of tax debts were also preferred debts. This could significantly impact on the potential for ordinary creditors to receive any payment at all. The preference for government debts has since been repealed.

Ordinary debts are the debts remaining. However, it is possible for some debts to be "postponed" so that they will not be paid until the ordinary debts have been paid in full, with interest. Such debts include certain loans based on the share of a partnership's profits and loans from spouses.

Supervision

The Accountant in Bankruptcy has a general supervisory role in the bankruptcy process. In addition, a trustee can take advice, and must follow guidance, from creditors and commissioners.

Commissioners are elected by creditors specifically to supervise the trustee. It is unusual to have commissioners in modern bankruptcies.

A trustee is also subject to the general supervision of the sheriff court. A trustee must apply to the sheriff for permission to undertake certain actions. A trustee may also apply to the sheriff for guidance. Most decisions of the trustee can be challenged by interested parties via an appeal to the sheriff.

Restrictions placed on a bankrupt debtor

During the period of their bankruptcy, an individual debtor faces certain restrictions on their conduct. The period of a bankruptcy is from the "date of sequestration"[2] until the debtor is discharged.

The restrictions include:

- A ban on a debtor obtaining credit of £2,000 or more without disclosing their bankrupt status. Where a debtor already has debts of £1,000 or more, they cannot obtain further credit without disclosing their status.

- A ban on holding certain elected offices, including being an MP or an MSP.

- A ban on being involved in the management of a company (unless the debtor has the permission of the court).

Bankruptcy may also impact on the positions a person can hold, or the jobs they can do. For example, someone cannot practise as an insolvency practitioner or a solicitor while they are bankrupt.

Bankruptcy restrictions orders

The Accountant has the legal power to impose a bankruptcy restrictions order. A sheriff may also impose a bankruptcy restrictions order.

Such an order may be considered where a debtor has acted dishonestly or recklessly either before or during their bankruptcy. An example of behaviour which may give rise to a bankruptcy restrictions order would be continuing to trade when the debtor knew a business was unable to

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[2] This is either the date when the Accountant in Bankrupt awards bankruptcy in a debtor application or when the court grants a warrant to cite a debtor to appear in a creditor petition.

meet its debts. An order may also be imposed were a debtor fails to co-operate during the bankruptcy process.

A bankruptcy restrictions order imposed by the Accountant can last between two and five years. A bankruptcy restrictions order imposed by a sheriff can last between five and 15 years. The effect of a bankruptcy restrictions order is to continue the restrictions an individual faces during the period of their bankruptcy. These are discussed above.

Sederunt book

The trustee is required to keep a record of the administration of a bankrupt debtor's estate. At the end of the process, relevant documents are collated into a record known as the "sederunt book". Trustees send the sederunt book to Accountant in Bankruptcy staff, who check to ensure that all relevant information has been included. ,

Accountant in Bankruptcy staff hold onto the sederunt book for six months. It is then passed to the National Archives for Scotland.

Discharge

Under the 1985 Act, discharge from bankruptcy was automatic. At first it happened after three years, and latterly (under provisions brought in by the Bankruptcy and Diligence etc. (Scotland) Act 2007) after one year. On discharge, a debtor's liability for almost all the debts they had incurred before they were made bankrupt ends. The restrictions which apply to accessing credit etc. are also lifted.

Only a very small number of debts survive bankruptcy. These include court fines, student loans and liabilities arising from fraud or breach of trust.

However, the Bankruptcy and Debt Advice (Scotland) Act 2014 removed automatic discharge. It is now up to the Accountant whether a debtor will be discharged. Normally, this will happen shortly after one year. But, where a debtor has not co-operated during the bankruptcy process, discharge can be postponed. The Accountant's decision is subject to review and may be appealed to the sheriff.

A debtor who has been made bankrupt under the MAP process is automatically discharged after six months. However, they are subject to some restrictions (including the restriction on borrowing more than £2,000) for a further six months.

A debtor who has been made bankrupt under the full administration process may be discharged after one year. However, they will still be required to make contributions from income beyond this period (for at least three further years). They will also be required to declare any assets they acquire in the next three years to their trustee. Ownership of the assets will automatically pass to the trustee.

OTHER STATUTORY DEBT SOLUTIONS

BACKGROUND

There are three options laid out in legislation for people who cannot pay their debts. Bankruptcy is one of them. The others are the protected trust deed and the Debt Arrangement Scheme (DAS).

Bankruptcy and protected trust deeds are both insolvency procedures. Once a debtor has gone through an insolvency procedure, their liability to repay any debts included in the process ends. This is sometimes called “debt relief”. Such debts are described as being “written off”.

DAS is not an insolvency procedure. Instead, it provides a structure for debtors to pay back their debts in full over a longer time period (although it is now possible for some DAS plans to contain an element of debt relief).

A further significant advantage of using a statutory debt solution is that creditors are prevented from taking action to enforce their debts. This can include things like seizing wages in the hands of an employer or money in a bank account.

It should be noted that many debtors rely on an informal agreement with their creditors to repay debts at a reduced rate, rather than pursuing one of the statutory options. This can be known as a “debt payment plan” or “debt management plan”.

The advantage of the informal approach is that it is very flexible. However, creditors are not bound to agree to – or stick to – informal proposals. Even where an agreement is in place, a creditor can decide to pursue full payment at any point. This makes it an unstable option.

There are also other non-statutory options for dealing with debts, such as remortgaging or taking out a consolidation loan.

Not repaying a debt as agreed is likely to have an impact on a person’s (or organisation’s) credit rating. Most defaults will be recorded on their credit record. This may mean that they will not be able to access credit in the future (including a mortgage). Alternatively, they may only be able to access high-cost credit.

Accountant in Bankruptcy staff maintain a Register of Insolvencies (covering bankruptcies and protected trust deeds) and a DAS (debt arrangement scheme) Register. Creditors can access the information electronically. It is therefore very easy to discover whether someone has entered a statutory debt solution.

PROTECTED TRUST DEED

A “trust deed” is a voluntary agreement between a debtor and their creditors. It results in their income and assets being administered by an insolvency practitioner (known as a trustee) for the benefit of creditors.

The trust deed is a form of personal insolvency and is regulated by the Bankruptcy (Scotland) Act 1985. The process is very similar to bankruptcy, but without the various restrictions on entry. A debtor must owe at least £5,000 to enter a trust deed.

Trust deeds are available to individual debtors. They are also available to partnerships, trusts, and unincorporated bodies (eg. some clubs and associations). “Bodies corporate” may enter protected trust deeds, but not companies or limited liability partnerships.

When a trust deed becomes protected, creditors are prevented from taking court action against the debtor. In order to become protected, a majority of creditors are required to agree to the proposals contained in a trust deed. There are procedures for “deemed” consent where a creditor does not respond.

A trust deed does not need to become protected. It can continue as a binding agreement between the debtor and those creditors who agree. However, the debtor will not be protected by enforcement action from those creditors who have not consented. Nor will their debts be written off at the end.

It is therefore usually the intention that a trust deed should become protected. As noted above, a debtor (where they are an individual or a partnership) who has been unsuccessful in seeking protection for their trust deed can use this as a route into bankruptcy.

Protected trust deeds generally last for a period of four years. During this period, a debtor is expected to make contributions to their debts from income and/or assets.

After the agreed period, if the debtor has co-operated with the trustee, almost all outstanding debts are written off. This makes the protected trust deed a form of debt relief. The debts which are not written off are the same as in bankruptcy.

The trustee in a protected trust deed will usually sell any assets of value, including a debtor's home. However, it is possible for a debtor's family home to be excluded from a protected trust deed where there is minimal equity and the creditors agree.

The trustee will charge a fee for administering a protected trust deed which is paid out of the debtor's estate. This reduces the money available to be distributed to creditors.

It also means that a debtor has to have some disposable income (or other assets) to enter a protected trust deed. Otherwise, an insolvency practitioner will not be prepared to administer it as they will not get paid. Thus, those on low incomes may not be able to access protected trust deeds.

DEBT ARRANGEMENT SCHEME

DAS is a statutory scheme enabling people to make reduced payments towards their debts under a "debt payment programme" while being protected from court action by creditors. It was introduced by the Debt Arrangement and Attachment (Scotland) Act 2002.

DAS can be described as a debt management option rather than a debt relief option because debts are not automatically written off as a result of participation. Instead, DAS is designed to allow debtors to repay their debts in full over a longer period of time.

As a result, those with insufficient disposable income to repay their debts in full (eg. because they have a low income or a high level of debt) are not able to use DAS. They must consider another way to deal with their debt situation.

When a debtor enters DAS, interest and charges accruing on their debts are frozen for as long as the programme remains in operation. In addition, debts can be written off where creditors agree and a debtor has participated in DAS for 12 years and paid of 70% of what they owe.

DAS is administered by Accountant in Bankruptcy staff. Access is free to debtors, although those who choose to work with a private sector money adviser may pay a fee for these services. Both the Accountant in Bankruptcy's office and the agencies responsible for distributing payments to creditors take a percentage of the funds distributed to cover their costs.

Creditors can object to a debtor's repayment proposal. In these circumstances, the Accountant applies a "fair and reasonable" test to decide whether to give approval to the debt payment programme. Unlike other statutory debt solutions, debtors are not required to sell any significant assets (such as a home or valuable car) as part of their participation in DAS.

Business DAS

Originally, DAS could only be used by individual debtors. However, the Scottish Government has recently introduced a “business DAS”, which enables certain other entities to take advantage of paying their debts over a longer time. A business DAS is available to partnerships, trusts and unincorporated bodies (such as most clubs and associations). It is also available to corporate bodies (but not companies or limited liability partnerships).

Business debt payment programmes can last for a maximum of five years. This means that if an organisation cannot repay its debts in full in five years, it will not be able to use the scheme.

Those entering a business DAS must take advice from an insolvency practitioner. The insolvency practitioner must certify that the organisation remains financially viable.

RECENT LEGISLATIVE REFORM

The Bankruptcy (Scotland) Act 1985 has been heavily amended. This is the main reason why consolidation is being considered. A brief history of the main legislative reforms is provided below.

THE BANKRUPTCY (SCOTLAND) ACT 1993

Among other things, this made provision for the Accountant to act as trustee in certain cases. Previously, the government was responsible for meeting the fees of trustees in small personal bankruptcies where there were insufficient assets in the debtor’s estate to cover the costs.

A large increase in the number of such bankruptcies had been causing a significant drain on public funds. Allowing the Accountant to act as trustee was intended to reduce these costs.

THE DEBT ARRANGEMENT AND ATTACHMENT (SCOTLAND) ACT 2002

This did not technically deal with bankruptcy. However, it did create the Debt Arrangement Scheme as a statutory debt solution. DAS had some of the advantages previously only available through bankruptcy. These included the ability to require creditors to participate in the scheme, and preventing them from taking action to enforce payment of their debts.

THE BANKRUPTCY AND DILIGENCE ETC. (SCOTLAND) ACT 2007

This legislation made sweeping reforms to bankruptcy, as well as the options available to creditors to enforce their debts. Key changes included:

- Reducing the length of time it took to be discharged from bankruptcy, from three years to one. The policy rationale for this was to encourage entrepreneurship.
- Creating bankruptcy restrictions orders.
- Enabling debtors to apply for their own bankruptcy to the Accountant rather than the courts.
- Introducing the LILA route into bankruptcy for low income debtors. It has since been replaced by the Minimal Asset Process. Debtors using this route did not have to demonstrate “apparent insolvency”.
- Giving the Accountant the power to supervise trustees in protected trust deeds.

THE HOME OWNER AND DEBTOR PROTECTION (SCOTLAND) ACT 2010

This made several reforms designed to ensure that debtors would not lose their homes where this could be avoided. The intention was to mitigate the expected impact of the recent recession.

The 2010 Act introduced the “certificate for sequestration”. This gave debtors who could not demonstrate apparent insolvency a route into bankruptcy. At the time, there were debtors who could not pay their debts and could not enter the LILA route into bankruptcy (eg. because they owned their home). Some of these debtors wanted to become bankrupt but were prevented from doing so because no creditor had taken court action against them.

The 2010 Act also allowed a family home to be excluded from a protected trust deed. This is only possible where there is minimal equity in the property and where all the creditors agree.

THE BANKRUPTCY AND DEBT ADVICE (SCOTLAND) ACT 2014

The purpose behind the Bankruptcy and Debt Advice (Scotland) Act 2014 was to better integrate the three statutory debt solutions. At the same time the bill was introduced, regulations to amend the protected trust deed and DAS processes were also brought forward.

The main changes made by the 2014 Act were:

- To require an individual debtor to seek money advice before applying for their own bankruptcy. Money advice was already necessary before entering a protected trust deed or DAS.

- To standardise the way a debtor’s surplus income was assessed. Surplus income is used to repay creditors. The Common Financial Tool (described above) is the method used to do this. The same system is used across all three statutory debt solutions.

- To extend the period a debtor would have to make contributions from income from three to four years in bankruptcy. Regulations made the same extension for protected trust deeds. Any assets acquired by a debtor in the four years after their bankruptcy (or their entry into a protected trust deed) would also become the property of the trustee.

- Freezing a creditor’s ability to enforce debts when a debtor indicates that they intend to apply for a statutory debt solution. This is also known as a “moratorium on diligence”. The 2014 Act made such a moratorium possible in relation to bankruptcy and protected trust deeds. It already existed for DAS. It allows a debtor a six week break to decide how best to deal with their debt situation without the threat of enforcement action by creditors. As long as a debtor applies for one of the statutory debt solutions before the end of the six week period, their protection will continue.

- To introduce the Minimal Asset Process route into bankruptcy for low income debtors.

- To remove automatic discharge from bankruptcy so that debtors who did not co-operate with the process could have their discharge delayed.

- To transfer a number of decision-making powers from the courts to the Accountant. The Scottish Government characterised all the processes involved as administrative, but there was much debate during the passage of the 2014 Act about whether this was the case.

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RELATED BRIEFINGS

SB 13-60 Bankruptcy and Debt Advice (Scotland) Bill

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