OFFICIAL REPORT
AITHISG OIFIGEIL

Economy, Jobs and Fair Work Committee

Tuesday 21 March 2017

Session 5

The Scottish Parliament
Pàrlamaid na h-Alba

Tuesday 21 March 2017

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ECONOMY, JOBS AND FAIR WORK COMMITTEE
10th Meeting 2017, Session 5

CONVENER

*Gordon Lindhurst (Lothian) (Con)

DEPUTY CONVENER

*John Mason (Glasgow Shettleston) (SNP)

COMMITTEE MEMBERS

*Jackie Baillie (Dumbarton) (Lab)
*Bill Bowman (North East Scotland) (Con)
*Ash Denham (Edinburgh Eastern) (SNP)
*Richard Leonard (Central Scotland) (Lab)
*Dean Lockhart (Mid Scotland and Fife) (Con)
*Gordon MacDonald (Edinburgh Pentlands) (SNP)
*Gillian Martin (Aberdeenshire East) (SNP)
*Gil Paterson (Clydebank and Milngavie) (SNP)
*Andy Wightman (Lothian) (Green)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Mike Dailly (Govan Law Centre)
Richard Dennis (Accountant in Bankruptcy)
Graham Fisher (Scottish Government)
Alan McIntosh (Govan Law Centre)
David Menzies (Institute of Chartered Accountants of Scotland)
Paul Wheelhouse (Minister for Business, Innovation and Energy)

CLERK TO THE COMMITTEE

Alison Walker

LOCATION

The David Livingstone Room (CR6)

Scottish Parliament

Economy, Jobs and Fair Work Committee

Tuesday 21 March 2017

[The Convener opened the meeting at 09:34]

Decision on Taking Business in Private

The Convener (Gordon Lindhurst): Good morning, and welcome to the 10th meeting in 2017 of the Economy, Jobs and Fair Work Committee. I ask everyone to turn their electrical devices to silent or turn them off if they are likely to interfere with the sound system.

The first item of business is a decision on whether to take item 3 in private. Are we agreed?

Members *indicated agreement.*

Subordinate Legislation

Bankruptcy Fees (Scotland) Regulations 2017 (SSI 2017/37)

09:34

The Convener: The next item of business is consideration of the Bankruptcy Fees (Scotland) Regulations 2017. I welcome our first panel of witnesses: Mike Dailly, principal solicitor at the parliamentary and social policy unit of the Govan Law Centre; David Menzies, director of insolvency at the Institute of Chartered Accountants of Scotland; and Alan McIntosh, project manager of the personal insolvency unit of the Govan Law Centre.

Do any committee members have interests to declare?

Bill Bowman (North East Scotland) (Con): I am a member of the Institute of Chartered Accountants of Scotland.

John Mason (Glasgow Shettleston) (SNP): I am also a member of ICAS.

The Convener: Thank you. Both Mike Dailly and David Menzies have submitted papers to the committee. I ask Mike Dailly to start us off with the principal points that he would like to make about the regulations that we are considering today. I will then ask the same of David Menzies. We will then move to questions from committee members.

Mike Dailly (Govan Law Centre): Thank you, convener. I thank the committee for inviting Govan Law Centre to give evidence this morning on the bankruptcy fees regulations. I will briefly summarise the concerns that Govan Law Centre has regarding the regulations.

It is worth noting that the stated policy objective of the regulations is to ensure that the bankruptcy fee structure in Scotland remains appropriate and fair. In our respectful view, the notion that fee increases of almost 200 per cent can be appropriate or fair does not make any sense. We believe that the proposals are regressive, unfair and punitive.

To take one quick example, under the current rules, the Accountant in Bankruptcy charges a fee of £2,800 on the repossession sale of a family's home that has £60,000 of equity. Under the regulations, those fees would rise to £8,000, which represents a 183 per cent increase. It is important to remember that the £8,000 in that scenario would come in addition to the cost that a homeowner in Scotland would have to pay in legal expenses during that process—which could be many thousands of pounds—and in addition to the costs of the sequestration. I see many people who

have been made bankrupt because they owe, for example, £3,000 or £4,000 of council tax or tax generally. They will end up with possibly £15,000 to £20,000 in general fees for sequestration.

Here is the point. What is the justification for that massive increase? As far as we can see, primarily it is to subsidise the AIB's deficit, due to the drop in cases over time—those are its own costs—and, to a smaller extent, to cross-subsidise the cap on the fees that the AIB charges to insolvency practitioners. Our concern is that that is not fair. At the end of day, where is the value for money in that process? The process is ultimately being paid for by Scottish consumers.

Finally, we think that the policy will have unintended consequences. I fear a situation in which somebody is sequestrated and they have equity in a house that is going to be repossessed—unless we can defend them, and we defend many people. However, let us say that the house will be repossessed and the fee hikes have gone through. The chances of that person or family getting some money back out of their equity would be substantially reduced. That means that their ability to have sufficient money, for example, to pay a deposit on a private rented flat or to get back on their feet and buy a property that is cheaper will be diminished. That has the implication of more homelessness applications to local authorities.

The public costs have never been factored in by the AIB or in the impact assessment. The only thing that has been missing in the impact assessment is the impact on the people of Scotland. That is our concern.

We are calling for a full review of the way that the AIB is funded, so that we do not have this piecemeal approach. It is not sustainable. Thank you, convener.

David Menzies (Institute of Chartered Accountants of Scotland): I, too, welcome the opportunity to present evidence to the committee on the statutory instrument. The committee has already received my letter to the convener, in which there was a lot of detail. It is important to recognise that the AIB is a public body and that statutory fees are necessary. We are not opposed to statutory fees—they are a necessary part of the AIB's operational income. The issue is how the fees are made up.

It is important for the committee to understand that statutory fees are ultimately payable by the end recipient of the process. In the main, that is likely to be creditors, because they either receive a dividend or do not receive any dividend at all. However, as Mike Dailly alluded to, there are occasions when there is a reversion. That means that all the assets are realised, all the creditors are paid in full and some of the debtor's estate is left over, which goes back to the debtor at that point. The fees are payable by the creditor or, in the latter circumstances, the debtor.

The total Government fees, or take, out of the costs of bankruptcy are quite substantial. Most personal insolvencies are not VAT registered as the people are private individuals. By the time that the 20 per cent VAT has been added on, as well as the 17.5 per cent audit fee from the AIB and the other statutory fees, the costs of the insolvency process are probably increased by something in the region of 40 to 45 per cent, which is a substantial increase in the burden on the estate.

The fee proposals that have been put forward are significant percentage-wise in many instances, but it is recognised that some of that is relatively small in terms of monetary value individually. For example, an increase from £19 to £50 is not a huge amount in pounds, but it is a fairly significant percentage increase.

It is likely that the burden of the creditor fees will be felt by other areas of the public purse. In particular, it is likely to affect Her Majesty's Revenue and Customs and local authorities, and the fee increases will be paid by them. Approximately two thirds of individual petitions of sequestration are made by HMRC or local authorities so the increase in the petition fee will be felt predominantly by them.

We welcome the cap on the AIB audit fee on practitioners, which is a step in the right direction. However, the cap of £5,000 will affect very few cases and it will certainly not affect the AIB's income. If need be, I am happy to provide examples of the complete unfairness of the audit fee and of the lack of value for money that it provides.

The regulations also provide for interest to be charged on late payment of fees. That came as a surprise to us, as there was no mention of that as part of any consultation process. We are not necessarily opposed to interest being charged. It is absolutely right that interest should be charged when an insolvency practitioner firm does not pay the amounts that are due when they are due. Our issue is with the consultation process and the interest level that will be charged. The 8 per cent interest level has been described by the minister as punitive and that is probably correct. If we consider the current low level of interest rates, that level is not sustainable. The interest must not become another source of funding for the AIB and it should be reserved for cases in which there is a need to take further action against someone who has not met their obligations.

We are now in a new position of historically low personal insolvency rates. My expectation is that

the low level will continue for a considerable time and I do not think that we are ever likely to get back to a situation in which 22,000 or 24,000 people per year are declared bankrupt in Scotland. I guess, therefore, that we could have an ever-decreasing circle, with the impact on fee income requiring a further increase in fees as we go on. Such a position is just not sustainable.

I agree with Mike Dailly that now is the time for a fundamental review of the funding of the agency and the setting and structure of fees. I think that there is also some conflict of interest in the AIB with regard to functions being duplicated and carried out elsewhere, and its role and function cannot necessarily be ignored in the setting of the fee regime.

09:45

The Convener: Thank you. I will bring in Mr McIntosh as and when, but at this stage we move to questions from members. Anyone who wishes to comment on or respond to those questions should indicate as much by raising their hand.

Richard Leonard (Central Scotland) (Lab): I wonder whether Mr Menzies can develop a little bit more his very last point about a potential conflict of interest in the Accountant in Bankruptcy's role as practitioner and as policy adviser.

David Menzies: ICAS has had this concern for many years now. The agency has a large number of functions that conflict with each other. For example, it acts as policy adviser to the Scottish Government and a quasi-regulator of the profession; it has supervisory duties that, I think, conflict with the policy advice situation; and the fact that it also provides accountancy services must conflict with its policy advice role. Beyond that, as well as carrying out and supervising cases, it acts as decision maker and appeals adjudicator in many instances. It is all fine and well saying that Chinese walls can be put in or that teams can be separated, but the actual building in Kilwinning is not that big, and it must not be possible to keep everything completely separate and apart down there. Those conflicts of interest must therefore exist.

Some of the agency's functions are, I would guess, superfluous. Its regulatory function, for example, comes from the Bankruptcy (Scotland) Act 1913, and regulation has come a long way since then. As you are probably aware, the primary act was, up until last year, the Bankruptcy (Scotland) Act 1985, which was brought in a year before the licensing of insolvency practitioners was introduced. Given that we now have a fully robust regulatory regime for insolvency practitioners, what is the purpose of having another layer of regulation as carried out by the AIB? What does that add to the process? Those additional layers and conflicts of interest certainly lead to additional costs in the overall process.

The Convener: I ask committee members and witnesses to keep their questions and answers as succinct as possible, because our time is fairly limited. I call Jackie Baillie.

Jackie Baillie (Dumbarton) (Lab): I will try to be very brief, convener.

We understand that 533 bankruptcy awards have been made through creditor petitions from HMRC, which amount to 38 per cent of the total. How likely is it that HMRC will withdraw and seek the services of private insolvency practitioners, as it has indicated that it might?

David Menzies: As you said, HMRC has certainly indicated that it is looking at the option; indeed, from discussions that I have had with HMRC officials, it is a real prospect.

Jackie Baillie: I was also quite interested in your comment that local authorities and HMRC account for two thirds of petitions. In that case, do you think that local authorities are likely to follow suit?

David Menzies: Some have already done so. For instance, Glasgow City Council now has a panel, if you like, that prefers to put such matters out to a private trustee rather than the AIB. I would imagine that other local authorities are likely to follow suit.

Jackie Baillie: Let me ask the obvious question: what will that do to the future sustainability of this kind of fee structure?

David Menzies: It is just not sustainable in this simple form.

Alan McIntosh (Govan Law Centre): One of my biggest fears is about what will happen now. We have seen this before; in fact, I would describe insolvency law and the fee structure almost as a complex algorithm, in which tweaking one bit can have unintended consequences.

We saw such consequences as early as 2012, when the cost of low-income, low-asset bankruptcies was raised from £100 to £200 and there was a sharp drop-off in the number of people who were able to access them. That has now been reversed; we introduced a minimum asset procedure in April 2014, and the fee has come down to £90.

My concern is the unsustainability of the Accountant in Bankruptcy going forward, given the reducing case load and the policy of full cost recovery. Eventually, the AIB will have to start hunting for fees in other places. Maybe we will come back in a year or two to look at how much it will cost a debtor to apply for bankruptcy, and we

will then be considering a fee of £300 or £400 rather than £200. That would create barriers and raise issues around access to justice.

Prior to 2008, someone who was on an income-based benefit would get a fee waiver from the Scottish Legal Aid Board because the process was done through the courts. That is no longer possible. One of the reasons that there was a massive spike in bankruptcies in 2008 was because the Bankruptcy and Diligence etc (Scotland) Act 2007 removed one of the legal obstacles—apparent insolvency—that had prevented a lot of debtors from being able to go bankrupt. There is a danger that we will start to replace legal barriers with financial barriers and obstacles for people, and that creates a big issue around access to justice.

Jackie Baillie: I have one tiny question. All of you said in your submissions that there should be a full review. As a starting point, do you believe that there should be full cost recovery?

Mike Dailly: That goes back to Richard Leonard's point, and David Menzies's comments, about the conflict in interest in the policy resting with the AIB.

The answer to your question is no, and I will outline the real challenge. In the rest of our legal system, there is fee remission based on income in the courts—and even in employment tribunals, although the fee situation for accessing tribunals is not great. There is no such remission for people seeking to access the AIB. How can that be right? If we accept that the AIB undertakes some quasi-judicial functions that used to take place in the sheriff court but have now been passed on, we must recognise that, ordinarily, someone on a low income would not have to pay fees. However, people have to pay fees to access the AIB. Why is that? The reason goes back to the point about the conflict of interest. The AIB sets the policy, and that cannot be right.

Access to justice, in which the AIB is involved, goes back to the Magna Carta and habeas corpus. I was involved in some of the work that led to challenges on fees, because we did not have fee remission in Scotland for a very long time. That leads us back to the constitutional right in Scotland, and in the rest of the United Kingdom, that means that when someone accesses justice, they are not accessing a commodity in the sense of buying a tin of beans, in which they would have a choice. Often, they are accessing justice because they have no choice, so there must be an element of someone who is very poor or on a low income being able to access justice without being hit with charges.

Andy Wightman (Lothian) (Green): Have any of you done any calculations of the impact on the AIB's forecast deficit if the regulations do not proceed and we continue with the existing instrument? The policy note describes the impact as

"£1.3 million in 2017-18, £4.2 million in 2018-19 and £3.0 million in 2019-20".

Alan McIntosh: The business and regulatory impact assessment notes with regard to fees such as the commission for recovering heritable property—the house issue; obviously the audit fees are different—that the benefits will be passed on to the AIB's agents. The AIB does not always administer a lot of bankruptcies; it has agents that it instructs to do that. Therefore, I do not know whether, and how much, the AIB would benefit directly from the fees, or whether the benefit would simply go to its agents.

David Menzies: I do not have access to figures that would allow me to do that calculation. A lot of that depends on information that only the AIB currently has, so I am not able to assess that specifically. I would imagine that the impact of not making the change would be exactly as the AIB has set out in the policy statement with regard to the level of fees.

Mike Dailly: We should think about the real world for everybody else, whether public bodies or charities working in the third sector. We have all had to deal with cuts and absorb the pain of austerity. The AIB seems to be one of the few bodies—if not the only one—in the country that is in a bubble.

Our concern is about who is paying for this. It cannot be right that if somebody has paid their mortgage all their life and has ended up going through hard times and trauma, the AIB then comes along and take its 188 per cent increase from the equity on their house.

Alan McIntosh: The business and regulatory impact assessment identifies the people who will be impacted as being the creditors and insolvency practitioners, which I find disturbing. In the past week I have dealt with two cases from citizens advice bureaux in South Lanarkshire and Ross and Cromarty that involve young women who have homes with young children in them. In one case, if the young woman's house is sold, the amount going to the AIB will increase from £2,500 to £6,750. In the other case, if the house is sold, the increase will be from £3,400 to £9,500. In both those cases, there would be a reversion of funds to the debtors, but those people would lose their home. In terms of vulnerability, bankruptcy does not get any harsher than that—someone with children losing their home.

In cases such as that, the fee increase that people will see will be dramatic. The policy document says that ultimately the cost of

bankruptcy or sequestration is "borne by the creditors", but that is absolutely untrue. In cases such as the two that I have described, the cost is borne by the debtor. Those people are paying 100p in the pound back to their creditors, they are paying the cost of the administration of their bankruptcy, they are losing their home and they are paying the 8 per cent statutory interest on their debts, which the minister himself has described as punitive, and now we are going to introduce massive increases. It seems blatantly unfair.

David Menzies: I will put that in context. About 4 per cent of all sequestrations per annum result in a reversion back to debtors, which equates to about 260 individuals.

Gil Paterson (Clydebank and Milngavie) (SNP): On the point that Mike Dailly made, as I understand it, you are looking not for a review, but for a suspension of these regulations and for the Government to come up with a new system.

Mike Dailly: That is right. The regulations have been laid and this committee is the lead committee, so I suppose that, technically, it would have to reject them—I do not know the terminology. If that is not done, clearly we will have a difficulty. You are absolutely right.

Gil Paterson: My other question is about the percentage of those who are not paying or are slow paying. If the figure should not be 8 per cent, what would you suggest is a more reasonable figure?

Mike Dailly: I remember discussing the issue at a round-table session when Hugh Henry was the justice minister. He agreed with us and, as my colleague Alan McIntosh said, Paul Wheelhouse, the current minister, agrees with us as well.

Goodness me, nobody is getting 8 per cent at the moment—look at any savings account. The UK banks have reduced the rates on ISAs, for example; you get a better rate on a savings account if it is not an ISA, because the base rate is at 0.5 per cent.

Sometimes it takes years and years before these cases are fully wound up. The percentage has to be above the base rate, but we could look at other jurisdictions. I ask Alan McIntosh to describe the situation in Ireland.

Alan McIntosh: I am also an insolvency practitioner in the Republic of Ireland, which has always been tied to us and has had the same 8 per cent rate that we have had in the UK. In December, the Irish Government reduced judicial interest and statutory interest to 2 per cent.

David Menzies: A number of years ago, a Law Commission report looked at the judicial rates of interest and suggested pegging them to the base rate, at about 1.5 per cent above it, so the rate would fluctuate.

Gil Paterson: Why do you believe the rate of insolvencies will remain slow?

David Menzies: There has been a realisation in the creditor community. Ultimately, the creditor community is made up, in the main, of commercial businesses, and they want to get back as much as possible. However, they recognise that, in this day and age, it is better to work with the debtor to get something back than to get nothing back out of bankruptcy at the end of the day. The Financial Conduct Authority's regulatory system on treating customers fairly has a big impact on how creditors deal with debtors. There is certainly now no rush to declare somebody bankrupt.

You will see from the figures that the majority of bankruptcies are actually voluntary—they are led by the debtor rather than the creditor—and, unless there is some sort of social change, I do not expect any change in that. Everyone is predicting that there might be a small increase in insolvencies over the next few years, but the level will certainly not be anywhere near back to the 22,000 or 24,000 a year that we saw six or seven years ago.

10:00

Alan McIntosh: One reason for that 24,000 figure, which was maybe 10 years ago, was that legal obstacles were removed through the Bankruptcy and Diligence etc (Scotland) Act 2007, which allowed people to go bankrupt. There was a build-up of people, and there was a build-up of historical debt. We have actually dealt with a lot of that historical debt very well in Scotland. In fact, there have probably been in excess of 160,000 insolvencies since 2008. When we compare Scotland with a jurisdiction such as Ireland, which has a very antiquated insolvency system, we find that it is still trying to deal with its historic debt from the pre-credit-crunch era. In Scotland, we have been very effective and successful in doing that. We now have other remedies such as the debt arrangement scheme, which allows people to avoid using insolvency—I agree with David Menzies on that.

Gordon MacDonald (Edinburgh Pentlands) (SNP): I want to ask Mike Dailly about his written submission, which says that there has been "no significant reduction" in staff costs or overall AIB costs in the past nine years. However, do you not accept that the information that you give does not reflect any inflationary increase? In 2008-09, AIB expenditure was £12.4 million. Using the Bank of England's inflationary calculator suggests that, in 2015-16, that would have been £15 million, when the actual figure was £12.2 million. Do you not

accept that there has been a cut in the AIB's operating costs over that period?

Mike Dailly: I accept what you say—it is correct—but I argue that that applies to all public bodies. Actually, it applies across the board. My colleague Alan McIntosh made the point that, at the end of the day, it is real people who pay for this, and, typically, people have not had wage increases or perhaps they have had a 1 per cent wage increase. People who have ended up on social security benefits have had them frozen. The third sector and the public sector have experienced that real cut and, of course, the Scottish Government has experienced massive cuts in its budget, which have all been passed on, including of course to local government.

The point is: why should the AIB be any different from councils, non-departmental public bodies, charities or businesses? For somebody running a private business whose case numbers and income dropped, if they simply tried to double their fees, they would discover that, in a competitive and open market, people would say, "Actually, I'm not going to use your business—I'll use somebody else."

That again comes back to Richard Leonard's point about conflicts of interest. People cannot use another organisation—that is the problem. We have created this creature, if you like. It does a lot of good work—we are not saying that it does not—but, because of all the conflicts, it has ended up in this mess of a situation.

Gordon MacDonald: I am not disagreeing with anything that you are saying; I am just trying to get the background to your figures—that is all.

Mike Dailly: Sure.

Gordon MacDonald: On AIB staff numbers, at the very high peak of 22,410 insolvencies, there were 140 staff, and the organisation currently has around 140 or 145 staff. However, immediately before that peak, back in 2006-07, when the number of cases was running at about 6,000 a year, the staff figure was still 140.

Are you saying that there is too much slack in the system? How did it cope with that peak when the staff levels seem to have been more or less consistent, although they did go up a wee bit during 2008 and 2009?

Alan McIntosh: Possibly. When we compare figures with 2006, we must always factor in the fact that the insolvency system in Scotland has dramatically changed. We have seen massive improvements in software, with the Basys, Astra and Dash systems, and we are moving away from clerical to online applications. With the Bankruptcy and Debt Advice (Scotland) Act 2014, we have seen a lot of additional administrative roles being placed on to the free sector and advisers. When we make comparisons, we need to realise that there has been a lot of moving of the furniture and a lot of technological advancement. Therefore, we would expect to see a reduction in the time required to administer cases and in the cost involved—that has to be taken into consideration.

Mike Dailly: In the rest of the public sector in Scotland, because there is a Scottish Government no redundancy policy, what happens in practice is that posts are not filled when people retire or move out into a different sector or completely. Lots of organisations have to operate with unfilled posts. Staff costs are normally the biggest outlay, so they have had to do that in order to cope with their budget settlements. The AIB is not doing that and—not to labour the point—our concern is that it is perverse that that comes at the expense of very vulnerable people.

Gordon MacDonald: Finally, given the vast reduction in the number of cases, has there been any change in cases' complexity?

David Menzies: I would not say that there has been any substantial change.

Bill Bowman: David Menzies said at the beginning that there were conflicts of interest within the AIB. If those were to be resolved, would that add extra cost, or are there other bodies that could take over some of those functions in respect of regulation or whatever he was thinking about?

David Menzies: We now have a very robust regulatory system for insolvency practitioners in the UK. That licensing system has been there since 1986 and works pretty well. The AIB's currently regulatory function is historical, under the Bankruptcy (Scotland) Act 1913, from when we did not have the current regulatory system. There does not seem to be any real function now for the AIB, in duplicating the regulatory system. If that was taken out, I imagine that elements of cost would go out with it. I have no idea how much—the public accounts do not disclose that on a divisional reporting basis—but the logic is that there must be an element of cost that could be removed.

Bill Bowman: Therefore, the conflicts could be resolved without putting in place yet more cost.

David Menzies: Yes.

John Mason: To follow on from Gordon MacDonald's line of questioning, are you clear how much of the AIB's costs are fixed costs—a cost base that is inevitably the same whether it has 10 cases or five—and how much are linked to the actual number of cases that it has?

Mike Dailly: We have talked about the numbers of staff remaining the same, and we have provided evidence—as has the AIB, on an annual basis—of

the number of cases dropping quite substantially. That must mean that the costs per case have shot up, so it is perhaps no surprise that the fees costs are going up. However, we see that happening in that way as being very unfair. Other public bodies are not in a position to do that—other public bodies can charge fees, but we have not seen the same hike in relation to local authority processes, registration fees and so on in the public sector. The situation is very peculiar, and we think that it is because of those issues of conflicts and because, in effect, the AIB is operating within that bubble. That is why we say that the AIB needs to be looked at in the round.

John Mason: I get that. However, it would maybe be fairer if I ask the AIB about that.

Govan Law Centre's figures show that the fees would be £4,500 for £30,000 of equity and £8,000 for £60,000 of equity—so, roughly double. I assume that the cost to the Accountant in Bankruptcy is not double because the estate is double. Is that the case?

Alan McIntosh: I will give an example. A person in their 30s and a person in their 60s could live next door to each other in exactly the same kind of house. There is an issue of equality that the business and regulatory impact assessment has not really dealt with, because it does not identify debtors as people who will potentially be impacted, and so equality issues have maybe been missed. If one person's house was sold, they could have only £10,000 of equity because they had a mortgage. The AIB would take £1,500 because that would be 15 per cent of the £10,000 of equity. However, the person next door might have £100,000 of equity, because they have worked all their life and paid off their mortgage, and they would have to pay £10,000.

The approach is obviously disproportionate, because it is based on equity. The cost of selling both houses would be the same and the bankruptcy administration work would be the same, but the person with the equity, who could be elderly—that is more likely to be the case—would pay a disproportionately bigger cost under the system. Ultimately, there is a sliding scale.

John Mason: The argument will be that it is about the ability to pay, but we can take that up with the Minister for Business, Innovation and Energy.

The minimum fee is £1,500. Should I take it that that would not cover the Accountant in Bankruptcy's costs?

Alan McIntosh: It is a commission-based system. I think that that would be in addition to the costs of selling the property. Maybe David Menzies can confirm that.

David Menzies: That is correct. The basic fee, which is the first fee that is listed in the schedule, is a fixed cost, no matter whether there are assets or no assets in a case.

John Mason: As an accountant, I would think that if I did an audit, it would be for so many hours at so many pounds an hour. Is there any relationship with that approach?

David Menzies: In the policy paper, the AIB set out how it came up with the figure. It is basically its fixed cost divided by the number of cases and multiplied by the four years—

John Mason: So we are back to fixed costs again.

David Menzies: Yes.

John Mason: They are not the case costs. Okay, that is helpful.

David Menzies: It is a basic, fixed-cost fee.

John Mason: Okay. I will pursue that later.

The Convener: Do committee members have any other questions?

Dean Lockhart (Mid Scotland and Fife) (Con): I understand that the fees that we are discussing relate to the bankruptcy of individuals, sole traders and partnerships. Can you give me a rough breakdown of those? I do not need the detailed numbers but, if we are looking at 4,000 cases this year or last year, what would be the breakdown of bankruptcies of individuals, partnerships and sole traders?

David Menzies: I am not sure. I certainly do not have access to that information, but I think that the Accountant in Bankruptcy would be able to provide it.

Dean Lockhart: I think that most bankruptcies are voluntary after debtors have received advice from money advisers. Do you have a rough idea of the proportion of individual bankruptcies that are voluntary versus the proportion who are forced into it?

Alan McIntosh: Voluntary bankruptcies might be as much as 80 to 90 per cent of bankruptcies—or in the high 80s. Maybe fewer than 10 per cent are not. A couple of years ago, the figure was 86 per cent. I do not know whether David Menzies has a more up-to-date figure for voluntary bankruptcies. There has been a complete reversal from the situation around 30 years ago.

David Menzies: In the last fiscal year, there were only 3,765 creditor-led actions. They are certainly in the minority.

Dean Lockhart: Right. What is the main cause of people seeking voluntary bankruptcy? What is the main trigger?

Alan McIntosh: Usually, it is going to a money adviser. Obviously, people who have financial difficulties go to money advisers. The Bankruptcy and Debt Advice (Scotland) Act 2014 brought in the requirement that people now need to receive advice before they can go bankrupt. I think that most people would go to a money adviser, who would look at all the options, including the debt arrangement scheme. A debtor could apply for their own bankruptcy as the best option for them on the advice of a money adviser or insolvency practitioner. I do not think that such cases would usually be affected by the big fee hikes in realising assets, because most money advisers would not advise a person to go bankrupt if that meant losing their home. They would look at another option, such as the debt arrangement scheme. I think that creditor petitions, where creditors take court actions to force people into bankruptcy, would primarily be impacted on.

The Convener: I thank all three of our witnesses very much for coming to the meeting. That concludes this part of our evidence session.

10:15

Meeting suspended.

10:20

On resuming—

The Convener: Welcome to the second half of this morning's session on the Bankruptcy Fees (Scotland) Regulations 2017. I welcome Paul Wheelhouse, the Minister for Business, Innovation and Energy.

The Minister for Business, Innovation and Energy (Paul Wheelhouse): Good morning.

The Convener: The minister is accompanied by Graham Fisher, who is head of branch in the constitutional and civil law division of the Scottish Government's legal directorate. Unfortunately, Richard Dennis, who is the chief executive of the Accountant in Bankruptcy, has been delayed in traffic. We have discussed the matter with the minister, and I think that he is happy for us to commence without Mr Dennis.

Paul Wheelhouse: Fingers crossed.

The Convener: There is a representative from the AIB present in the room, who should feel free to pass notes to the minister if there is any issue on which he needs assistance during the session.

Have you seen the submissions from ICAS and Govan Law Centre, minister?

Paul Wheelhouse: I have.

The Convener: Good. Those submissions raise a number of issues, which will undoubtedly be covered by members of the committee. You will be given an opportunity to respond and comment on matters as they develop.

The rate of interest of 8 per cent that the regulations propose to introduce has been raised. In the ICAS submission, you are quoted as saying that that "seems punitive". As Graham Fisher will be aware, the judicial rate of interest is 8 per cent, and that seems to have been the basis for the proposal in the regulations. In a courtroom situation, a judge can modify the rate of interest that applies, but I do not think that there is a similar provision for modification in the regulations that we are considering.

The issue of the rate of interest was considered by the Court of Session more than four years ago, on 20 February 2013, in the case of Farstad Supply AS v Enviroco Ltd. In upholding a decision by a lower court judge to reduce the rate to 4 per cent, the Court of Session judge said in paragraph 31 of his judgment:

> "it is plain that the mismatch between the judicial rate and interest rates prevailing in the financial world which has existed following the crisis of 2008 is a matter of concern."

Why is the Government thinking of introducing a rate of 8 per cent in the regulations? What are your views on the matter, given that the courts have expressed concern about the fact that the judicial rate of interest, on which the rate that is proposed in the regulations seems to be based, is so high?

Paul Wheelhouse: That is an important point, convener. I had intended to address a number of points in my opening remarks.

The Convener: Please do.

Paul Wheelhouse: I think that that would be helpful.

I will start by addressing the point that you have raised. You correctly cited my view that the judicial rate of interest is too high in the current context. We anticipate that the UK Government will undertake a UK-wide consultation on the judicial rate of interest. We hope to learn from that and to adapt the rate that applies in Scotland accordingly. If that does not happen—it is taking longer for the process to get started than we had anticipated—we will have to review our position and perhaps take a lead on the issue by adopting an approach that is unique to Scotland. However, we are still of the view that that UK-wide consultation will take place and that, in due course, we will benefit from the input of stakeholders on the appropriateness of using a judicial rate of interest of 8 per cent as the basis for such decisions.

I acknowledge that the rate is high, although the rate that is applied is not applied across a large number of cases. Two debtors account for 59 per

cent of the aged debt—debt that is due for more than 30 days—that we have on the books. The total is more than £230,000, and about 80 per cent of the aged debt relates to protected trust deeds.

Given that funds are gathered for only one month of the time when the trust deed is protected, we believe that the argument that they should be paid from an insolvency firm's own funds should not really hold true. There is an issue around court fees such that, if statutory fees were applied, there would not be a question about the need to pay quickly.

I will now go through my opening remarks, convener.

The Convener: Yes—please do.

Paul Wheelhouse: Perhaps I will then bring in Mr Fisher, who has some knowledge of the case to which you referred.

Thank you, convener, for the opportunity to address the committee this morning. The regulations before you update and replace the Bankruptcy Fees (Scotland) Regulations 2014. For the most part, they apply to bankruptcies arising from debtor applications made or creditor petitions received on or after 3 April 2017, and protected trust deeds granted on or after that date. Previous fees will continue to apply to pre-existing cases—it is important to make that point.

I believe that there is a clear case for the regulations to come into force in their current form. Ensuring that the people of Scotland have access to fair and just debt relief processes is a key priority for the Scottish Government, and I believe that we have a strong track record in that regard. The Accountant in Bankruptcy is the office-holder responsible for those processes. Oversight of the AIB's role and performance is a ministerial responsibility for my portfolio, and I am of course accountable to Parliament for ensuring that the funding and administration of insolvency strike the right balance between drawing upon public funding and generating fee income to help with cost recovery.

I believe that it can be shown that the AIB achieves that balance. In my view, we have a personal insolvency regime that stands favourable comparison with any other in the UK. By way of context, in 2016-17 the AIB's Parliament-approved budget was £2 million after the spring budget revision. Forecast reductions in operational income, which are due to changes in the number and composition of cases, mean that the public funding requirement will increase to £4.2 million in 2018-19. In that context, it is worth stressing that the measures introduced in the regulations will provide only an estimated £207,000 of additional income to help offset any further requirement for additional public funding.

The question is whether the balance between extra funding from the taxpayer and extra income from creditors is the correct one. Clearly, continued efficiencies within the AIB will play a vital part in minimising the impact on the taxpayer. The AIB's staff figures show that there were 173 full-time-equivalent staff in 2009-10, but that that had dropped by 20 per cent to 139 in 2015-16. I am aware that the committee has seen papers from other witnesses, but I stress that, in our view, they do not accurately represent the change in personnel numbers in recent years.

Over the equivalent period, the AIB's funding requirement from the Scottish Government has reduced from more than £4 million to the current position. Furthermore, it is important to note that, in the past three years, the AIB has introduced three major public-facing information technology systems, all on time and within budget. Each of those has the specific aim of simplifying procedures, reducing administrative effort and increasing efficiency in processes, not only for the AIB but for money advisers, debtors and insolvency practitioners.

The AIB has taken on additional tasks following legislation passed by the Scottish Parliament. Reforms introduced in 2015 implementing the Bankruptcy and Debt Advice (Scotland) Act 2014 resulted in new functions being conferred on and transferring to the AIB. The aim was partly to reduce burdens elsewhere in the system, not least the Scottish courts.

The AIB now considers applications for recall of bankruptcy, the award of shorter-term bankruptcy restriction orders and applications to cure defects in procedure. Those functions were all previously the preserve of the court, but there has been no increase in resource or staffing to support that increased workload. It is not just that staff numbers have been falling, but that that has happened in the context of new responsibilities and of IT investment having been successfully deployed.

Turning to the cost of administering bankruptcy procedures, I am aware of some of the concerns that have been raised by witnesses relating to the fees charged and the realisation of assets. I note those concerns. However, as the committee may already be aware, the administration costs that are charged by the AIB for insolvency cases in Scotland are significantly lower than those that apply elsewhere in the UK, and they will remain very considerably lower even after the proposed changes.

10:30

I will now set out the relevant differences from the approach taken in England and Wales and in

Northern Ireland, which are two separate jurisdictions for our purposes today.

Where assets are realised, the sums that are potentially available to creditors in Scotland far exceed the equivalent figures in England and Wales. I would be more than happy to provide further information to the committee to support that. I believe that a table might have been provided to the committee this morning, and I hope that that will be helpful in our later debate. The AIB has made a firm commitment to ensuring that debt relief mechanisms in Scotland are accessible and that financial barriers to entry are minimised, in recognition of the fact that it is often the most vulnerable in society for whom debt relief and insolvency present the only real option to provide a fresh start.

In April 2015, the AIB introduced the minimal asset process, which is a low-cost mechanism to access bankruptcy for those with few assets and no disposable income. The fee that is charged in Scotland for that scenario is £90. The general up-front fee to access bankruptcy in Scotland is £200. By comparison, in England and Wales, the up-front fees that have to be met by debtors are £680, which is 240 per cent higher than in Scotland, and, in Northern Ireland, the fee is £640, which is 220 per cent higher than in Scotland. The up-front costs for petitioning creditors are very considerably lower in Scotland. Those costs are £563 here, as opposed to £1,270 in England and Wales, which is 126 per cent higher, and £850 in Northern Ireland, which is 51 per cent higher.

It is worth stating that, when we look at realisation of assets, we can see that the overall cost of administration, including commissions, are considerably lower. In Scotland, that might amount to £3,936, or 39 per cent, for realising £10,000 of heritable assets, whereas an equivalent process under the Insolvency Service in England and Wales would amount to £8,292, or 83 per cent. That represents a 43.5 per cent difference in the share of the asset value taken in England and Wales.

For a £100,000 asset, the difference is less eye-watering, but costs in Scotland are still substantially lower, with the effective cost being 13.9 per cent of the asset value realised in Scotland, compared with 21.8 per cent in England and Wales, which means that 7.9 per cent less of the asset's realised value is taken in Scotland.

We are conscious of the need to keep costs down where we can do so, and I think that it is important that we continue to preserve low-cost access to debt relief for debtors and, with no proposed increase, the regulations do exactly that. I believe that the regulations set out a sensible and equitable approach that reflects the challenging context for public finances and adapts to changing case numbers, but which supports the continuation of fair and just debt-relief mechanisms in Scotland.

No one would choose to increase fees without good reason. However, the fact remains that the costs require to be met and my belief is that it would be unfair to instead levy further up-front costs that would act as a barrier to access to debt relief in the first place. It would equally be unfair to put all of this at the door of the taxpayer. The fees regulations, coupled with on-going efforts to achieve efficiency savings, represent the most effective approach, while leaving far more of the asset value after costs than is the case in England and Wales.

My colleagues—I should more properly say "colleague", at this point, of course—and I are happy to answer any questions or expand further on the points that I have raised in this introduction.

I apologise for the long statement, but I hope that it was helpful.

The Convener: Thank you for the statement, which gave the context for your position.

Jackie Baillie will ask the first question.

Jackie Baillie: I would like to explore the issue of creditor petitions. We have heard evidence this morning that HMRC and local government account for something like two thirds of creditor petitions. We also heard that HMRC is seriously considering withdrawing from using the Accountant in Bankruptcy and instead seeking assistance from insolvency practitioners in private practice. That course is also being followed by local authorities. That makes me wonder about the sustainability of the AIB, given that, as prices and charges increase, customers will go elsewhere.

Paul Wheelhouse: Those are important points. It is a pity that Mr Dennis is not here to address them. I know that he has had discussions with HMRC around those matters, which we have also discussed in ministerial meetings.

We are trying to maintain a balanced, competitive fee structure. Clearly, HMRC works effectively with the AIB, and we value that relationship. We would look to discuss and understand HMRC's concerns, but I do not anticipate that there is any immediate issue. It is not necessarily anything that we would need to take into account.

Mr Dennis has just made a timely arrival. For his benefit, I state that we are discussing the issue of creditor petitions, the dominance of HMRC with regard to the work that is done through the AIB, and its threat to withdraw from working with the AIB.

I believe that the package that we propose today is proportionate. It is about striking the right balance between taxpayer funding of the AIB service and reflecting the drop in the number of cases in particular categories, along with the need to cover the cost of the organisation. We do not want to reduce the organisation's effectiveness by continuing to see the number of staff fall. We need to get that balance right, and I think that we have proposed a proportionate system that will ultimately deliver more for the creditor and, I hope, leave some assets for the debtor once the creditors have been paid. That is less likely to be the case in England if 82 per cent of the value of a £10,000 asset is taken by costs, fees and commission before the creditor even starts to be paid back.

Jackie Baillie: Can I push the minister a little bit on that? Now that Mr Dennis has arrived, he might be able to help you.

Paul Wheelhouse: Indeed. A white knight is on the horizon.

Jackie Baillie: I am genuinely interested in whether there is a plan B. If HMRC withdraws and local authorities seek alternative arrangements, that will be a big chunk of the AIB's work gone. Do you then take that monetary value and spread it among the debtors, or is there a different plan B?

Paul Wheelhouse: I take the point entirely that we need to prepare for such a scenario, although I hope that it will not unfold. I will bring in Mr Dennis because, as I said earlier, he has been discussing the issue.

Richard Dennis (Accountant in Bankruptcy): My apologies to the committee. I was held up on various motorways in the snow.

Am I right in thinking that Ms Baillie is picking up on the comments in the minutes from HMRC suggesting that it might look to appoint its own trustees?

Jackie Baillie: Yes, and the evidence that we heard from ICAS this morning.

Richard Dennis: That evidence quoted those minutes. You will be aware that creditor petition fees come in two parts: £150 is paid up front and £300 is paid if the AIB is appointed as trustee. HMRC's suggestion was that the increase to £300 might cause it to think again.

However, that is extremely unlikely to come to pass. We make a loss on the majority of creditor cases, so HMRC would have to find someone who was ready to take that work on. We also pay a substantially higher dividend when the AIB is trustee in comparison with when there is a private trustee. Around 20 per cent of the dividend goes back to creditors. I would be very surprised if HMRC managed to find IP firms that were ready to take on the work for just an extra £300. As I say, we make a loss on these cases, so if HMRC can find someone else to do them, that is all to the good.

Jackie Baillie: Is HMRC sabre rattling?

Richard Dennis: I suspect that it was giving its initial reaction to the proposals that were put in front of it. No one likes to see fee increases. It is fair to say that I would like to go back to the office and consider options, but I think that that is all that HMRC was saying.

Jackie Baillie: We have no guarantee that it, or local authorities, will continue to use the AIB.

Richard Dennis: We have no guarantee, but, as I say, we deliver a better service in terms of returns to creditors and our costs are lower than those of most insolvency practitioners. That is partly because insolvency practitioners take on more complicated cases. HMRC tends to be a very aggressive creditor and it does not always pursue the more complicated cases.

The Convener: Mr Dennis, the minister was given an opportunity to make some comment on the ICAS and Govan Law Centre submissions. Do you want to make some preliminary remarks now that you are here or are you happy to respond to questions from committee members? I am content either way.

Richard Dennis: Thank you, convener. As you are already short of time, I will answer questions. If I may have an opportunity to come in with anything that I want to add at the end, that might save time.

The Convener: Thank you. The minister referred to a fee structure table that was sent to the committee this morning and has now been passed to members.

Ash Denham has a question.

Ash Denham (Edinburgh Eastern) (SNP): Minister, you will be aware that we took evidence this morning from Mike Dailly of Govan Law Centre. I just want to get your comments on a couple of his remarks, if I may.

Mike Dailly said that the policy objectives should be for the fees to be appropriate and fair and that he feels that some of the increases do not meet those objectives. He gave the example of a case in which there was home equity of £60,000 and said that the fees would go up from £2,800 to £8,000, which is a 183 per cent increase. He also said that, in those cases, the money left in that equity that would allow people to start over—and such people could be in substantial hardship—would be reduced. What are your comments on that?

Paul Wheelhouse: Nobody takes these decisions lightly. I have certainly had discussions with the Accountant in Bankruptcy around the issue, because I know that there are great sensitivities. This may not be commonly known, but I went through the situation as a child, as part of a family that lost their home through debt, so I do not take the issue lightly, believe me. The example of £60,000 is given in the table that we have provided today. There is a slight difference with the figures in Mike Dailly's table, as he is starting from a slightly lower point—if you add in all the fees, commissions and so forth, you get a different starting point. We are not denying that there is a significant increase in fees, but we still end up in a position where, after the changes that we are putting in place, £4,227 more is left for either the creditor or the debtor than is the case in comparable jurisdictions, such as England and Wales. We are trying to be proportionate. We are conscious of the fact that, as Mr Dennis has said, we are not fully covering the administrative costs of cases and will make a loss, but we are trying to ensure that at least the pressure on public resources is managed as well as possible. We are mindful of the impact on individuals in the—thankfully—relatively small number of cases in which eviction is required, and there are safeguards to try to protect people in hardship and to prevent the unnecessary loss of their family home.

I ask Mr Dennis to comment, as he may be aware of the kind of scenario that Ms Denham has described, and may be able to give some guidance on how that would be handled in practice.

Richard Dennis: It is worth repeating that it is a tiny minority of cases that involve any assets at all. The vast majority of bankruptcies produce nothing for anyone. I have some figures that show that the changes in commissions would have affected less than 1 per cent of cases in 2015-16.

Gillian Martin (Aberdeenshire East) (SNP): In submissions to the committee and in the evidence from the previous panel, people have highlighted their belief that there is a conflict of interests for the AIB, given that, as David Menzies's correspondence states, it is also a

"policy advisor to the Scottish Government, quasi-regulator, provider of trustee services and decision maker and appeal adjudicator.

Could Richard Dennis respond to that?

Richard Dennis: I will say two things in response to that. First, we have just finished an extensive programme of bankruptcy reform, which the Parliament has discussed at great length, and the decision to transfer powers from the courts to the AIB was a result of the 2014 act, which is now being taken into the consolidation. That followed an extensive period of consultation, so Parliament went into that knowingly and with its eyes open.

Secondly, whenever the AIB takes a decision, we take powers out of the courts, but we leave the backstop of appeal to the sheriff. We moved powers out of the courts because the AIB is less intimidating for people who want to seek a review. We are far quicker and we are cheaper, but that does not stop people going to the sheriff for a review if they do not like our decisions and reviews.

Gillian Martin: You mentioned the consultation. Quite a lot of creditors would be small businesses. Was there any consultation that included the views of the Federation of Small Businesses or other organisations that represent small businesses?

Richard Dennis: The consultation that I was referring to was the one that was carried out in the run-up to the big bankruptcy reforms that culminated in the Bankruptcy and Debt Advice (Scotland) Act 2014. We have a representative on the debt and insolvency services stakeholder forum; I believe that the committee has had a paper from the Scottish Parliament information centre listing the members of that forum. I do not think that the FSB is in there. The spokespeople for small creditors tend to be from credit unions, which are strongly opposed to practically all debt write-off for obvious reasons—they already struggle to afford loss of investment. However, small businesses are most unlikely to be affected by the big changes in fees.

Gillian Martin: The first panel of witnesses this morning are asking for another full consultation. What are your views on that?

Richard Dennis: In terms of the AIB's conflict of interests, I would say that we have already committed to reviewing the impacts of BADAS in full. Bankruptcy cases can take four or five years to run through, so it is slightly too early to look at the impact of the act, but nothing has come up that was not foreseen.

The safeguard exists but has not been used: no one has been through an AIB review for reconsideration of a case and, after that, gone to the sheriff. The options exist but are untested, which suggests to me that the system is working as intended.

10:45

John Mason: I want to return to the point about the 8 per cent interest rate, which the convener raised. You said that there is going to be a review at UK level of the judicial rate of interest, which is also 8 per cent. If that review brought the UK rate down to 6 per cent, would our rate automatically

go down to 6 per cent or is our rate fixed separately?

Paul Wheelhouse: There is no automatic link, but if the decision was made to reduce the judicial rate, I would work with the Accountant in Bankruptcy to review the rate that is applied in Scotland.

I return to the point that was made earlier: we are talking about a relatively small number of cases in which the interest rate is applied for persistent non-payment of fees and so forth. It does not apply across the board; it is used in a targeted way to encourage people who have a history of not paying to pay. We do not want people to lose the incentive to pay, but we would need to reflect on any decision that was made to change the judicial rate of interest and see whether that had implications for the rate that is applied here. I do not want to make the point too strongly, because there is no automatic linkage in the regulations, but we can return to the matter if there is a significant reduction in the judicial rate of interest.

John Mason: If the two rates are separate and we—or you—think that 8 per cent is too high, why are we waiting for the UK review? Why cannot we reduce the rate to 6 per cent, 4 per cent or 1.5 per cent above the base rate?

Paul Wheelhouse: I take that point, which also occurred to me. However, because the rate applies in a very targeted way, I do not know how many cases it would apply to. Perhaps Mr Dennis or Mr Fisher, who is aware of the court case that the convener referred to, can talk about the relevance. If the exercise that is undertaken at UK level concludes that the judicial rate of interest needs to be reduced significantly—given that the gap between the base rate and the judicial rate is, if not at an all-time high, substantially enlarged—we will want to reflect on that. I will ask Mr Fisher to comment.

Richard Dennis: Could I just make sure that we have understood Mr Mason's question correctly? Is your question whether, if the judicial rate of interest was reduced, we would automatically consider reducing the amount of interest that is charged on the late payment of debt, which is a separate issue?

John Mason: No. My first question was whether we would need to seek to change anything or whether the change would automatically work its way through. I got the fairly clear answer that it would not automatically work its way through.

Richard Dennis: That is right.

John Mason: You would have to make a conscious decision to do something, minister, although that would be one of the input factors.

Paul Wheelhouse: Yes. That is what I was trying to get across.

John Mason: If the change would not be automatic, I wonder why we are tied to the UK judicial rate of interest at all. However, I accept the minister's answer.

Graham Fisher (Scottish Government): It might be worth my saying something about the different contexts in which the interest rate is applied.

The convener made a few points about the fact that there is no discretion analogous to what the court has when the judicial rate is applied. However, I flag up the fact that we have added the provision in regulation 10(4) to allow the fees to be waived. The ICAS evidence, in particular, raised questions about the implementation of the interest rate, but, as the minister said, this is about only a very small number of cases in which there is persistent non-payment of fees.

The minister drew an analogy with court fees that are not paid. Under the regulations as they stand, trustees are bound to pay the fees at a particular time, and the new regulations are for cases in which the fees have not been paid. It would be possible to waive the fees in particular cases in which there was a problem. The rate of the fee, as it stands, is short of the rate in the Late Payment of Commercial Debts (Interest) Act 1998.

As I said, ICAS had asked for reassurances about implementation of the fee rate in practice. As the minister said, the matter has arisen in a couple of cases. He gave the example of two debtors accounting for 59 per cent of the debt that is due for more than 30 days as the only case in which the fee rate could be applied. On that basis, the fee rate and the ability to apply it would be implemented reasonably and interest waived if there was a reasonable excuse. The AIB has the ability to report trustees to the sheriff for censure where there is no reasonable excuse. That would apply in cases where fees have not been paid on the due date. I give the assurance that ICAS seeks that the fees would be applied reasonably.

The Convener: That would be entirely discretionary, so there would be no right—as there would be in a court case, for example—to apply to reduce the amount of interest.

Graham Fisher: There would be no right, but the AIB must consider the case. Furthermore, if the AIB made an unreasonable decision, that could be judicially reviewed just like any decision of an administrative authority. I take your point that no court would be directly involved, but we are talking about situations in which fees that should have been paid are past their payment time.

The Convener: Judicial review would not be a reasonable way of reviewing such a decision, because that would have to be done in the Court of Session. Surely the costs of doing that would be prohibitive in almost every case.

Graham Fisher: All that I have referred to is the fact that the AIB's freedom of action is constrained in setting the fee rates.

John Mason: Mr Dennis said that the AIB makes a loss on a number of cases. We have the scale of fees. I am assuming that where the fees are smaller, there is less equity and you make a loss, but that where there is more equity, you make a profit.

Richard Dennis: The vast majority of bankruptcies produce nothing.

John Mason: What is the cost of an individual case? Do the costs vary hugely?

Richard Dennis: The costs do vary hugely. If I was to guess off the top of my head, I would say that our administrative costs are about £1,500 a case.

John Mason: I presume that that is based on average hours worked at an hourly rate and suchlike. If you get £1,500, you will break even, although there would be fixed costs to take into account, too. Are you convinced that your fixed costs have been reduced as much as possible? That is the crux of some of the questioning. As you get fewer cases, the fixed costs must be spread among smaller numbers.

Richard Dennis: That is an entirely fair comment. It is perhaps of no surprise to committee members that, in every spending round, the Scottish Government puts agencies such as the AIB under huge pressure to make sure that it is not giving us more public money than it needs to. We have met the 3 per cent efficiency savings target that was set by the Scottish Government, and Audit Scotland has signed off our accounts every year since 2010. We are doing what we can to squeeze costs—

John Mason: Is that 3 per cent on top of the fall in case load—

Richard Dennis: Yes—it is 3 per cent against the budget that the Scottish Parliament votes for me.

John Mason: Is your budget falling in line with your reduction in cases and, on top of that, is there another 3 per cent reduction, or is your budget falling by 3 per cent?

Richard Dennis: My income from cases falls in line with the reduction in the number of cases. My budget is separate, because it is—kindly—topped up by the Scottish Government and the Scottish Parliament. I have to demonstrate a 3 per cent efficiency saving against my overall budget.

John Mason: As your case load falls and you get less income, you get more money from the Scottish Government.

Richard Dennis: We can also put up fees. The crux of the matter is getting the balance right.

Paul Wheelhouse: That refers back to the points that I made in my opening remarks. I want to emphasise an example of efficiency that I mentioned. The public-facing IT systems that the Accountant In Bankruptcy has developed in the past few years have also helped insolvency practitioners, creditors and—I hope—debtors to save costs. The IT helps the client side, if you like; it also helps with the organisation's operational efficiencies.

Gil Paterson: I have a small question that goes back to the interest rate. I note that you said that the new regulations will give you the powers and discretion to waive fees. Will they also give you the ability to reduce the rate in some fashion—in other words, to vary it?

Paul Wheelhouse: I ask Mr Dennis to comment on that.

Richard Dennis: De facto, the answer is yes. Let us say that two large debtors who I would like to chase owe fees on a huge number of cases. If I were to charge 8 per cent on £100,000, and it was overdue for 120 days, they could say that they will do a deal: if I waive the fee on certain cases, or if I waive the interest, they will pay tomorrow. Either of those options would be fine. All we are doing is creating a stick to make people pay the core fees that are statutorily due and not stretch cases out for as long as they can.

Andy Wightman: I have three questions. The first is for clarification from the minister. You mentioned in your opening remarks the sum of £207,000 to offset the forecast declines in operational income in the business and regulatory impact assessment—£1.3 million 2017-18, £4.2 million 2018-19 and £3 million 2019-20. To clarify, the £207,000 is the additional funding arising from the new fees—

Paul Wheelhouse: From the regulations.

Andy Wightman: —from the regulations that would offset that deficit in each of the years going ahead.

Paul Wheelhouse: I make the point that, in the absence of that, we would have to find a further £207,000 of public funding to top up the AIB's budget.

Richard Dennis: That is the amount that the increase will bring in the first year.

Paul Wheelhouse: That will grow to more than £800,000, I think, in the four years.

Andy Wightman: Thank you; that is very helpful.

Secondly, we heard evidence this morning that the impact of those fees, in the business and regulatory impact assessment, does not appear to take into account the behaviour changes that might arise among people making applications. Some people might be deterred, and that has not been properly taken into account. Given that they are people in fairly vulnerable situations, that is a pretty important impact. Do you want to comment on that?

Paul Wheelhouse: I will answer initially, and then I will bring in Mr Dennis. I have tried to emphasise that we are trying to avoid increasing up-front fees for debtors who seek help to address their issues. We want to allow people to act responsibly. Many people obviously want to sort their problems out, get their lives back under control and move on from whatever problems have arisen.

The up-front fees in England, Wales and Northern Ireland are much higher than they are in Scotland. We believe that we have, by avoiding putting them up, struck the right balance in recovering costs through realisation of assets. I want to emphasise that only in a very limited number of situations do we actually get anything from realisation of assets; where it does happen, we are leaving more of the assets for the creditor and, indeed, the debtor. We are trying to get it right at both ends of the equation through lower up-front fees and taking less of the asset value in the process. We are therefore bearing more of the cost of cases than is apparently the case in England, Wales and Northern Ireland. I think that that is the right balance. I will bring in Richard Dennis.

Richard Dennis: The minister has made the key point that we are not increasing debtor fees, which are the up-front fees, unlike our colleagues in England and Wales. The only people who might potentially be put off from seeking bankruptcy—it is a very significant step, and people should seek debt relief only if they genuinely need it—are the very limited number in whose cases the debts are covered in full, once the assets have been realised. In 2015-16, there were only 260 such cases.

Andy Wightman: My final point is that some concern has arisen as a consequence of the fact that the framework within which the fees are set appears to be rather arbitrary in terms of the forecast income of the Accountant in Bankruptcy and how much it feels it can recover in fees. The situation is different in other Scottish Government agencies. Registers of Scotland, for example, has full cost recovery. It puts aside funds in reserves when the property market is busy and draws on them when the property market goes down. In other words, it has a system in place to manage finances in the face of fluctuating income, and fee orders are then set by ministers according to a system that is fairly well understood. What we are discussing seems to be rather ad hoc decision making with very little framework around it to say how we set fees.

11:00

Paul Wheelhouse: In the AIB's defence, I say that it is difficult to predict how many people will run into insolvency or bankruptcy situations. We can have a rough idea of how the economy is going and make some predictions, but I would not want to rest entirely on them.

Registers of Scotland and other bodies attract fees from positive things—people transferring assets, which is a key part of market economy—and, therefore, raise fees in a positive environment. It would require significant investment by the Government up front to build up fees to the point at which we could provide an endowment or fund or, indeed, find funding to endow the AIB so that it had a float that would allow it to manage its finances over a period of time. I appreciate that the choice could be made to do that. Alternatively, we would have to significantly increase fees to allow a significant margin to be built up over time so that we could do that.

At the moment, we probably have the correct balance. Year to year we adjust the budget that the AIB needs to ensure that the balance is right between public funding for the core service that needs to be provided to help people who are in difficult circumstances, and recovering fairly an amount to repay some of the costs of administration without making a profit. At some point, we have to decide whether we want to take a market approach, in which we would free up the AIB to build up a war chest from cases—which might mean that we would have to have higher fees, as is the case in England—or continue with the balance that we have struck, which I think is right, and keep the costs down.

Andy Wightman: To be clear, I am not advocating that the AIB follow what Registers of Scotland does.

Paul Wheelhouse: I did not think that you would be.

Andy Wightman: I am just saying that Registers of Scotland has an understandable framework within which costs are allocated and fees are set.

Paul Wheelhouse: I believe that there is such a framework here. I appreciate that it does not have the same clarity or transparency as the relationship with Registers of Scotland that I described. We are trying to keep the balance right by ensuring that we provide enough funding and ensuring that reasonable costs can be recovered from cases without causing additional difficulty for the people who are affected by debt or, indeed, for their creditors.

The Convener: We are running on a bit longer than planned, minister. Is it all right if we ask a few more short questions?

Paul Wheelhouse: Yes.

Bill Bowman: I perhaps did not fully understand all the explanations. Earlier evidence was about the increase in the income from fees cross-subsidising other things that you do. Is that correct?

Paul Wheelhouse: I ask Mr Dennis to comment.

Richard Dennis: The answer is no. I think that the other evidence was about the fact that, in the package that is in front of the committee, we are imposing a cap on the audit fee, which we think will cost us about £86,000 a year in income. If we had left that fee without a cap and had the £86,000 coming in that way, we could have offset and reduced one of the other fee increases that we have proposed or we could have asked the Scottish Government to find us more money.

We have put together a package that we think is fair to raise about £800,000 in total by the end of the four-year period. It is certain that we will still need more funding from the Scottish Government to top up our budget in the coming spending round. I look forward to discussions with the minister, which I have no doubt will be trenchant, about how far he is prepared to go and the level of efficiency savings that he will expect us to deliver.

Bill Bowman: You mentioned new responsibilities coming to you from the recent act. Are you saying that they are fully funded elsewhere?

Richard Dennis: They are funded in the mix of our income; they are not being specifically funded from the fee increases. The new responsibilities were transferred to us in April 2015.

Bill Bowman: So some of the fee increase will go towards meeting them.

Paul Wheelhouse: I mentioned that point in the context of making it clear that staffing numbers had fallen while new responsibilities had been taken on. I say that just in case the committee has the impression that the staff numbers related only to casework. As has been discussed, the AIB performs other functions for the Government, including innovation with regard to all public-facing IT products. I was just trying to explain that I thought that the analysis of staff numbers that had been provided was unfair.

Gordon MacDonald: On the AIB's cost base, we have been given information this morning that, since 2009, your staff numbers have been reduced by 20 per cent while your case load has reduced by 63 per cent. Given the investment in new technology and IT that you have highlighted, are you satisfied that staffing is at the correct level?

Richard Dennis: As you would expect, broadly speaking, my answer to your question is yes. However, I should clarify that, on the case-load figure, it is the number of new cases that has fallen by 63 per cent. Most bankruptcy cases run for four or five years, so the stock has actually declined by far less than that.

Gordon MacDonald: What was the figure before and what is it now?

Richard Dennis: In our entire case load, which includes protected trust deeds and the debt arrangement scheme, there are—this is within a few thousand; I hope that the committee will forgive me—about 55,000 cases currently active, and there were about 65,000 at the peak.

Gordon MacDonald: So there has been a reduction, but it is probably more in line with the reduction in your staffing levels. Is that what you are saying?

Paul Wheelhouse: The figures that I have suggest that the total case load in 2015-16, which takes into account the historical cases that Mr Dennis referred to, had reduced by 5.6 per cent since 2010, whereas staff numbers had reduced by 19.6 per cent.

Gordon MacDonald: What would be the impact of annulling the regulations?

Paul Wheelhouse: We would have to find additional resources to make up the amount of up to £800,000 that is due to be recovered by 2020-21.

Richard Dennis: I hope that, if the committee recommended annulment, it would say which elements it disapproves of, and we would then bring forward a new package.

Paul Wheelhouse: Ideally, though, I encourage the committee not to recommend annulment, if it is at all possible. As Mr Dennis suggested, nobody likes to pay fees or the costs of such actions, but I hope that we have kept the right balance by not putting up up-front fees, which ensures that people who need support to clear their debts and get back on the straight and narrow can do so without any

disincentive. At the same time, we are not recovering as much asset value to cover our costs and commissions as is recovered elsewhere in the UK. Costs have gone up, as we have acknowledged; we are not taking the proposed action lightly, and we have tried to strike the right balance by reducing the take from the assets realised to ensure that creditors and, I hope, debtors get something back, if possible.

Richard Leonard: Govan Law Centre has a reputation as an organisation that fights for social justice, while the Institute of Chartered Accountants in Scotland does not—indeed, it is notorious as a revolutionary guard—but both have described your proposals, which are still before us, as unfair and regressive. We have to consider not how the fees compare with those in England and Wales but how they compare between this year and next year. As I read your proposal, the commission that is charged on assets realised is going to move from 15 per cent on the first £10,000 to 15 per cent on the first £50,000. Is that not an extraordinary increase?

Paul Wheelhouse: I would not characterise the changes in that way. I fully acknowledge the reputations of Govan Law Centre and of ICAS, both of which are good organisations that, in general, take different approaches. I do not take the points that they have made lightly, but I reiterate that we have to reflect the need to recover costs to some degree. We have held costs down to a substantially lower level than elsewhere in these islands in what is a similar economic and legislative context, although I acknowledge that we have our own jurisdiction in Scotland.

We believe that we are striking the right balance. We are not recovering the full costs, as Mr Dennis made clear, and we have not taken the decisions lightly. Even if ICAS and Govan Law Centre are not delighted with the changes that are going through, they have to acknowledge that the overall costs are far lower than they are in England and Wales, and the fees are far lower than those in England, Wales and Northern Ireland. We have the balance about right.

Richard Leonard: The issue is the scale of the rise—180 per cent overnight. That is a staggering increase, is it not?

Paul Wheelhouse: ICAS has said that it has "no significant objections" to the proposals. I take the point that Mr Leonard might have heard something during ICAS's oral evidence this morning that I was not present to hear, but that is what ICAS said in its submission.

The Convener: Does that not mean that it has specific objections?

Paul Wheelhouse: There is a particular issue about capping the audit fee, which was addressed in Mr Dennis's earlier remarks. I do not think that there has been a similarly strong objection to the costs that were set out in the table that we sent to the committee this morning.

Jackie Baillie: In his submission, David Menzies said:

> "The interest on unpaid fees provisions, which were not consulted upon, are not objected to in principle however the interest rate applied and the circumstances in which interest will be demanded do give cause for concern."

He went on to say that those things were not agreed and that ICAS felt that consultation was not sufficiently full.

Notwithstanding that, all the earlier witnesses said that they felt that a fundamental review was needed. I put it to the minister that having a fundamental review, rather than taking the piecemeal approach, might give everybody comfort and satisfaction.

Paul Wheelhouse: On the latter point, Mr Dennis made a good point about data and needing to have sufficient time to understand how the measures that we are putting forward will work in practice. I am happy to accept that we should sit down and do a performance review of the measures. If there were cases in which the impact on individuals was disproportionate, we would want to highlight them.

Some of the measures that we have talked about are provided as a disincentive, and I hope that the AIB can reach agreements with debtors to make sure that debts are paid without the need to invoke the relatively punitive interest rates that have been referred to. However, I take the point on board and, if we need to give a commitment to the committee to undertake a review at a suitable time and when we have the data to do that, I am happy to do so.

Jackie Baillie: So that there is no misunderstanding, I note that the witnesses talked about a review in advance of the regulations being put in place. They did not feel that there was sufficient justification for the proposals, and they felt that a more fundamental review of the approach was needed, rather than introducing the regulations and then reviewing them.

Paul Wheelhouse: It would be difficult to do a review before we had evidence of the impact of the changes that are to go through. However, I take Jackie Baillie's point about the impact. I hope that the clarity that we have been able to give today about the number of cases in which the interest rate would be applied and the relatively small number of cases in which there is a loss of a home or another asset has been of some comfort. We have also put in place safeguards to ensure that there is a right of appeal to a sheriff if people feel that they are being treated unfairly.

We are listening carefully to the views of the committee and we will take the points on board in considering our future policy direction.

The Convener: Mr Dennis, do you want to have a final word?

Richard Dennis: I have three quick things to say to the committee. On a fundamental review, Parliament looked extensively at all aspects of bankruptcy over a two-year period in the run-up to the 2014 act, including how we would charge. In the Protected Trust Deeds (Scotland) Regulations 2013, we introduced a different model for charging.

I suspect that the minister covered this in his opening statement, when I was not here to say it, but I put it on record that some of the things that Govan Law Centre said about my agency not delivering any efficiency savings were not true and that the staff numbers that it quoted were wrong. It looked at head count, not whole-time equivalents, in making some of its calculations.

We have made significant efficiency savings and have seen staff numbers reduced from about 170 to below 130 at the same time as taking on new responsibilities, and we expect staff numbers to fall further in the coming years. We are doing what we can to drive efficiency, and we also have an enviable record in delivering IT systems on time and under budget. There are not many chief executives who can say that.

11:15

I have talked about the package raising about £800,000 over the full four years. That is the level that we are looking to pick up in fees, out of about £12 million in current income. The big elements are the basic administration fee, which brings in about £400,000, and the up-front increase in creditor petition fees, which brings in about £250,000. As I am sure the committee is aware, up-front fees from the petitioning creditor can be reclaimed from the case, and I have not received a single representation from a creditor organisation—including all the big banks, which will pay the vast majority of those charges—to suggest that it is unhappy with the comparison between our proposed fee increases and those in England and Wales.

The Convener: You do not accept Govan Law Centre's figures on employee numbers. Will you give us the correct figures?

Paul Wheelhouse: I think that the number is down from 173 to 139.

Richard Dennis: The number of full-time equivalents in 2009-10 was 173. In 2015, the FT figure was 139. I can tell the committee that those numbers have declined further since the previous published figures, which we have cited because they are the figures that would be available to someone who looked at our published documentation.

The Convener: I thank our witnesses.

11:17

Meeting continued in private.

12:05

Meeting continued in public.

The Convener: Having discussed matters and considered this morning's evidence on the regulations, the committee will continue its consideration at next week's meeting. In the meantime, the committee will write to the minister to set out continuing concerns that he may wish to consider.

Meeting closed at 12:05.

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