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An t-Ionad Fiosrachaidh

Social Justice and Social Security Committee

17th Meeting, 2022 (Session 6), Thursday
26 May 2022

Inquiry into low income and debt problems – Issues paper

Purpose of this briefing

The purpose of this briefing is to highlight issues to discuss with the Accountant in Bankruptcy as part of the Committee's consideration of debt and low income.

This is the last formal evidence session featuring stakeholders.

The Committee is also working with a panel of people with lived experience of debt and low income to develop the outcomes of this inquiry. It is due to meet with the panel on 6 June. The Committee will then hear from the Scottish Government on 16 June 2022.

Background

Debt and poverty discussion

Background to the inquiry is outlined in the paper for the meeting on 12 May [Issues paper, 12 May 2022](#). This includes detail on the Committee's [informal meeting](#) in November 2021 and key issues arising from the call for views.

Legal framework

There are three statutory debt solutions in Scotland:

- **Bankruptcy** – where an individual's assets are managed (usually sold) by a trustee for the benefit of creditors. Once someone has completed the process, almost all remaining debts are written off. Minimal Asset Process bankruptcy

is simpler and quicker and can be used by people with low income and few assets. Full Administration Bankruptcy covers all other circumstances.

- **Protected Trust Deed** – a more flexible form of bankruptcy where the trustee is an insolvency practitioner in private practice. To enter a Protected Trust Deed, someone must have sufficient assets or income to pay the trustee's fees and offer some level of payment to creditors.
- **Debt Arrangement Scheme** – allows people to pay their debts in full over a longer period of time. There is very limited provision for debt write off in the Debt Arrangement Scheme, so people must have sufficient surplus income to pay their debts in the longer term.

Note though that most people in debt do not enter a statutory debt solution. Instead, they make reduced payments to debts through informal agreements with creditors.

Bankruptcy will be the main option for people on low incomes as they will lack any surplus income to pay fees or repay debts in full. However, there can be circumstances where a Protected Trust Deed or the Debt Arrangement Scheme could be used.

Work of the Accountant in Bankruptcy

The Accountant in Bankruptcy is both an agency of the Scottish Government and an office of the court. The Accountant in Bankruptcy is Richard Dennis and he heads up the Scottish Government agency of the same name.

The responsibilities of the Accountant in Bankruptcy (AiB) include:

- supervising trustees (insolvency practitioners) in bankruptcy and Protected Trust Deeds
- administering bankruptcies where no insolvency practitioner in private practice is appointed as trustee (around 80% of cases)
- administering the Debt Arrangement Scheme
- liaising with stakeholders and keeping the law in this area under review.

Following on from a recommendation from the Session 5 Economy, Energy and Fair Work Committee, the AiB has been undertaking a [review of statutory debt solutions](#) on behalf of the Scottish Government. There are three stages to this work:

Stage 1 looked at immediate changes to the law which could be delivered before the end of the Session 5 Parliament. This resulted in various reforms to bankruptcy law, which had originated in emergency coronavirus legislation, being made permanent. Changes included:

- reducing the fees to enter bankruptcy
- removing fees for people claiming certain social security benefits

- increasing the maximum debt threshold for a Minimal Asset Process bankruptcy from £17,000 to £25,000 and excluding student loan debts from this threshold.

Stage 2 looked at options for interim changes to statutory debt solutions.

Three stakeholder working groups looked at proposals in relation to the moratorium on diligence (a legally enforceable pause on creditors taking court action while someone in debt seeks advice), Protected Trust Deeds and bankruptcy. [The reports of the working groups were published on 13 May 2022.](#)

Three groups finalised their reports and recommendations, which will now be considered by the Minister for Public Finance, Planning and Community Wealth.

- [Introduction to the Stage 2 Working Groups Reports](#)
- [Group 1 – Moratorium and the Common Financial Tool](#)
- [Group 2 – Protected Trust Deeds](#)
- [Group 3 – Bankruptcy and cross-cutting issues](#)
- [Stage 2 Working Groups – Summary of Issues and Recommendations](#)

Several recommendations touch on issues considered by the Committee:

- that the minimum debt threshold to enter a Minimal Asset Process bankruptcy (currently £1,500) is removed to extend access to people with smaller debts, but there was no agreement on whether the threshold for full administration bankruptcies should be removed.
- that the moratorium on diligence is extended to include mental health crises, with further development needed to look at which mental health professionals should be involved in providing evidence
- that the AiB should do more to publicise the statutory debt solutions available in Scotland.

Stage 3 will consider more broadly whether statutory debt solutions meet the needs of a modern economy.

The AiB is also reviewing the framework for “diligence” (that is, court sanctioned debt enforcement used by creditors – such as seizing money in bank accounts). It expects to consult on reform proposals soon.

Witnesses have suggested changes to the law in this area – for example, increasing the Minimum Protected Balance in bank arrestments and making earnings arrestments more flexible.

Timescales

Legislation will be needed to implement many of the changes recommended at Stage 2 of the debt review. This would provide an ideal opportunity to incorporate recommendations from the Committee where they also required legislative change. However, it is not clear what the timescales for making changes is, and whether further consultation on Committee proposals would be needed.

Key issues

How to balance the interests of creditors and people with debt problems

The framework for debt enforcement and statutory debt solutions is commonly described as needing to balance the interests of creditors and debtors. Society needs to address the distress and economic harm caused by being unable to pay debts. But, ultimately, if creditors cannot enforce payment of debts, they won't be prepared to lend.

In its response to the Committee's call for views, the University of Aberdeen stressed the importance of balancing these interests – and that the legal framework must look at the interests of all people in debt, not just those with low incomes.

It noted that there is only so far that the legal framework for debt can go to address issues of low income. Overly focussing on this could result in a system which was not fair or balanced.

However, it was also argued that the Scottish Government's action on the legal framework for debt should reflect its wider priorities. Christians Against Poverty noted that it was unclear if the review had an "overarching policy intention of reducing poverty and improving outcomes for those on low incomes".

The Child Poverty Action Group stated: "Debt processes should support the Scottish Government national mission on child poverty, and the objectives of the statutory tackling child poverty delivery plan. They should be designed to avoid pushing children into poverty, deeper poverty or material hardship."

Access to bankruptcy

The Committee has heard about the role of "deficit budgets" for people with low income and debt problems. Money advice for people in this situation can be complex as there is no obvious solution. Options include grants from charities and negotiation with public sector creditors to reduce arrears payments so that the person can focus on current liabilities.

Bankruptcy is a potential option for people in this situation. Almost all existing debts will be written off by this process, relieving people of the burden of repaying them. However, it has been suggested that bankruptcy may only be a short-term solution as people will soon need to borrow again to make ends meet.

Some stakeholders have also suggested that bankruptcy may not be suitable for some low income money advice clients. Bankruptcy places limits on ongoing borrowing (and most consumer creditors will not be prepared to lend at all). Where someone who is in the bankruptcy process or has recently completed it needs to borrow to manage their budget, they may not be able to.

The Stage 2 debt review has recommended removing the minimum debt threshold to enter a Minimal Asset Process bankruptcy. This will improve access for people with smaller debts. Witnesses highlighted that making repayments to small debts could still trap people in situations of poverty and stress.

The working group could not agree an approach to the minimum debt threshold in full administration bankruptcy. Someone may need to access full administration bankruptcy if:

- they have debts greater than the Minimal Asset Process threshold of £25,000
- they own land or buildings (even if there is negative equity)
- they have individual assets worth more than the thresholds (£2,000 in total and £1,000 for an individual item).

The Stage 2 review also recommended more generous treatment of assets in Minimal Asset Process bankruptcies. It proposed that the £1,000 individual cap was removed, but no consensus was reached on the £2,000 overall limit.

Another issue raised with the Committee was the fact that currently, someone can only access a Minimal Asset Process bankruptcy once every ten years. The limit for full administration bankruptcies is once every five years.

Bankruptcy fees

Permanent changes to the law following coronavirus legislation reduced the fees to enter bankruptcy to £50 for Minimal Asset Process bankruptcy and £150 for full administration bankruptcy. Exemptions were also introduced for people receiving certain social security benefits.

However, respondents to the call for views highlighted that some of their low income clients still have to pay fees. Money advisers often have to spend time finding charities which will cover the costs of this for clients.

Having any form of fee to enter bankruptcy was described as “illogical” by several respondents. There were also suggestions that fees should be reduced further, or more exemptions introduced (for instance, for people assessed as having no disposable income using the Common Financial Tool¹).

¹ The Common Financial Tool is the system used to assess income across all three statutory debt solutions. It uses benchmarks of average expenditure by low income households in particular categories. However, people can provide evidence to justify certain additional expenditure in their particular circumstances.

In its submission, the AiB noted that, over the past year, 83% of Minimal Asset Process bankruptcies have not required a fee.

Debt enforcement

The AiB also plans to consult on changes to the law of “diligence” (formal, court sanctioned debt enforcement) soon.

Diligence statistics

The AiB produces statistics on how frequently different types of diligence are used. [The most recent statistics are from 2020 to 2021.](#)

The table below shows the number of diligences executed based on the procedure used to get court authority to take debt enforcement action. Activity decreased significantly in 2020/21 due to the coronavirus pandemic. However, 90% of diligences executed related to summary warrant for council tax.

Table 1: diligences executed by type of court procedure

Warrant procedure	2018-19	2019-20	2020-21
Summary warrant for council tax	239,535	240,890	114,545
Summary warrant for other public debts	6,315	5,600	1,390
Other court procedure	26,840	45,040	10,730
Total	272,690	291,535	126,665

Earnings and non-earnings arrestments are by far the most common types of diligence used by creditors. A non-earnings arrestment can seize a range of moveable asset in the hands of third parties. However, the vast majority are bank arrestments.

In 2020/21, 90% of non-earnings arrestments were for council tax debts.

Table 2: non-earnings and earnings arrestments by year

Type of diligence	2018-19	2019-20	2020-21
Non-earnings arrestment	191,680	218,305	92,060
Earnings arrestment	79,040	71,730	34,295

Bank arrestment

The Committee has heard concerns about the impact of bank arrestments from several witnesses and respondents to the call for views. Bank arrestments freeze money in bank accounts. Creditors are usually able to claim any money above the Minimum Protected Balance.

In the short-term respondents and witnesses would like to see the Minimum Protected Balance increased from £566.51 to £1,000.

In the medium term, respondents and witnesses would like to see more proportionate treatment of income above this sum – either by introducing a taper (so that only a percentage of income about £1,000 goes to creditors) or by giving consideration to household size. Note that banks, which currently have to administer bank arrestments without being entitled to a fee, are likely to be resistant to changes which make the process more complicated.

Earnings arrestment

The Committee has also heard concerns about earnings arrestments. These allow creditors to seize wages in the hands of an employer. Earnings arrestments can catch wages above £566.51 per month, with a varying percentage of the money above this (depending on how much the person in debt earns) being paid to creditors.

There have been calls for creditors to have clear scope to vary the amount of money seized in an earnings arrestment on their own initiative. This is intended to address the situation where someone has an earnings arrestment for council tax arrears which leaves them insufficient money to pay the current year's liability. This will usually result in the debt being enforced via summary warrant with a 10% surcharge.

There have also been calls for better co-ordination between different types of earnings arrestment. Usually, these will be combined (a "conjoined arrestment") so that the person in debt only faces one deduction, with the sums paid shared between creditors.

However, the Department for Work and Pensions has a relatively new power to seize earnings for social security benefit debts called a Direct Earnings Attachment. This power can also be used by local authorities in relation to Housing Benefit. Direct Earnings Attachments operate separately to the framework for other earnings arrestments, meaning someone can be left with less than the standard minimum protected sum.

Summary warrant procedure

The Committee has heard evidence that the process for enforcing council tax debts can be inflexible and have harsh consequences. Councils will often apply for a summary warrant after two instalments have been missed. This adds 10% to the total owed, increasing the burden of repayment for people on low incomes.

The Committee has not received any specific suggestions for reforming summary warrant procedure. The main call is for a more flexible and person-centred approach, potentially by introducing national guidance. There may also be potential to consider something similar to the pre-action requirements which are in place for rent arrears. These could require local authorities to refer people for advice, and to try to negotiate reasonable repayment offers, before they can progress to summary warrant.

Questions

Suggested issues to raise:

Theme 1: work of the AiB

- **Is there a time frame for introducing legislation to implement the recommendations of the Stage 2 debt review working groups?**
- **If the Committee makes recommendations which also require legislation what scope – if any – is there to integrate these into this work?**
- **What is the time frame for Stage 3 of the debt review?**

Theme 2: balancing the interests of creditors and people with debt problems

- **How much should statutory debt processes in Scotland be designed to improve outcomes for people on low incomes?**
- **Which of the recommendations from the Stage 2 reports do you think are relevant to the experiences of people with low income and debt problems?**

Theme 3: bankruptcy

- **We have had calls to remove the 10-year limit on applying for Minimal Asset Process bankruptcy as people on deficit budgets may run up debts again quickly. Is this something that the AiB would be prepared to take forward as part of the Stage 2 review work?**
- **Having any fee at all to enter bankruptcy could be argued to be inappropriate. What are the barriers to removing fees altogether?**

Theme 4: debt enforcement

- **What is the timescale for consulting on diligence reforms, and what issues is it likely to cover?**
- **Is there scope to increase the minimum protected balance in bank accounts to £1,000 as an immediate priority, outside of the consultation process?**
- **If not already covered – the Committee has heard calls for earnings arrestments to be more flexible and better co-ordinated. Will this feature in the consultation?**

- **The Committee has heard that council tax debt enforcement can be inflexible and harsh. Will options for improving this process form part of the consultation?**

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23 May 2022

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