How do you get money out of a Scotsman?

Stewart Rennie

I think the first answer that springs to mind is: “With great difficulty, especially if he’s at the bar”.

However the purpose of this talk is not to reflect on the events of last night but to consider the situation where you have been pursuing a debtor through the English Courts and now wish to enforce this in Scotland. I propose to give a quick run through the procedures for making your judgement enforceable in Scotland, pre-bankruptcy enforcement or diligence and finally the three main Scottish debt management routes, the Debt Arrangement Scheme (DAS), Trust Deeds for Creditors (the Scottish equivalent of IVA’s) and sequestration or bankruptcy. In particular I will consider the amendments made by the Bankruptcy and Diligence (Scotland) Act 2007 (the “BAD Act”).

Possibly the most basic point to convey is that the reason we have separate Scottish laws and courts is that they are guaranteed in terms of the Acts of Union of 1707 – it was a fundamental part of the original agreement to merge the Parliaments of the two countries that Scots law, churches and education remained separate. Scots law can probably now be described as a hybrid system but its roots are firmly in the Roman or civil law, as opposed to common law and this can throw up substantial differences e.g. you don’t need any consideration to constitute a contract under Scots law, you can’t create a security over chattels (or moveables as we call them) without possession and third party rights in contracts have always been recognised without the need for a separate statute. Every time I come down here I am surprised, and impressed, by the numerous references to cases, whilst we use them in Scotland it is definitely not to the same degree. More recently , since the passing of the Scotland Act 1998 we again have a separate Parliament which is sovereign over the areas devolved to it. This includes personal insolvency but not corporate insolvency. Finally I should point out that whilst we are a separate jurisdiction Scotland does remain part of the United Kingdom. I only say this because I was once phoned up by someone from Clifford Chance requesting a letter of opinion because “Scotland is a foreign country”. Whilst I am happy to issue an opinion on aspects of the Companies Act 2006 (as they insisted I do in this case) and to charge for it, it is something you can do yourselves.

However the fact that we are a separate jurisdiction does bring me on to my first point, once you have your judgement against the debtor from an English Court, how do you enforce this in Scotland. I am envisaging here the situation where either the debtor was originally resident in England or Wales and has since moved to Scotland or where the debtor has always resided in Scotland but the place of performance of the contract was in England or Wales and the contract was written under English law and accordingly you have brought an action in the English or Welsh courts. The first thing you need to render your judgement enforceable is a Certificate of Money

Provisions order under Section 18 and Schedule 6 of the Civil Jurisdictions and Judgements Act 1982 and Rule 74.17 of the Civil Procedure Rules. This provides:-
The judgment creditor may apply for a certificate by filing at the court where the judgment was given or has been entered written evidence stating –
(a) the name and address of the judgment creditor and, if known, of the judgment debtor;
(b) the sums payable and unsatisfied under the money provisions of the judgment;
(c) where interest is recoverable on the judgment, either –
(i) the amount of interest which has accrued up to the date of the application, or
(ii) the rate of interest, the date from which it is recoverable, and the date on which it ceases to accrue;
(d) that the judgment is not stayed;
(e) the date on which the time for appealing expired or will expire;
(f) whether an appeal notice has been filed;
(g) the status of any application for permission to appeal; and
(h) whether an appeal is pending.

Useful links can be found at:-

http://www.justice.gov.uk/civil/procrules_fin/contents/parts/part74.htm

and

http://www.scotcourts.gov.uk/you_and_us/faq.asp

Once you have obtained your Certificate of Money provisions you must register it in the Books of Council and Session in Edinburgh within 6 months of issue. This is a government register which I think is peculiar to Scotland. Once registered, the original document is kept there for all time and you are issued with an extract, which is the equivalent for all legal purposes to the original. This is called registration for preservation. However the certificate is also registered for execution which means that it is now the equivalent of a Scottish Court decree or judgement and can be used for enforcement purposes. The interesting point to note is that any deed can be registered for preservation and execution as long as the parties consent to this and accordingly it is possible to register Scottish loan agreements and guarantees for execution and to get an enforceable repayment order against a debtor without the necessity of going to court. You should therefore be very wary of any Scottish document that contains the term “and I consent to registration for preservation and execution” as that is all that is required to effectively grant judgement against your client.

Once you hold the extract order you have to send it to Sheriff Officers (the equivalent of Bailiffs) for enforcement. In terms of S9 of the Bankruptcy (Scotland) Act 1985 to found jurisdiction then the debtor must have been habitually resident or maintained a place of business within the relevant Sheriffdom at any time within the last year. Part of the aim of the BAD act was to reduce the administrative burden and cost of sequestration and since 1st April 2008 sequestration proceedings have only been

competent in the Sheriff Court, the Court of Session has been removed from the ordinary jurisdiction entirely.

However the purpose of the exercise is to get money out of the debtor and there are a couple of avenues that may be worth exploring before you move to sequestration. Not only may these result in payment they can also give you an advantage when you move to sequestration and can also run during any period that you are waiting to establish "habitual residence" for jurisdiction purposes.

In Scotland the procedure of enforcement is called diligence and the first diligence I want to mention is an Inhibition. This is similar to a charging order in that it is in respect of heritable or real property. The main difference is that it does not apply to a specific property but instead prevents the inhibited debtor from voluntarily alienating any heritable property owned by him in Scotland. Using the extract order you apply to the Court of Session for Letters of Inhibition, which are issued by the Session Clerk without the need for a hearing. The inhibition is served on the debtor and Letters of Inhibition are then registered in the Register of Inhibitions in Edinburgh. This is a public record that is always searched by the purchaser prior to completing any deal . Accordingly if an inhibition is registered against the seller the purchaser will not in practice go ahead with the purchase until the inhibition is lifted – the normal process is to deliver a partial or complete discharge of the inhibition at settlement of the sale transaction in return for a mandated part of the purchase price to clear or reduce the debt. Once registered an inhibition is valid for 5 years.

Further in terms of Section 37 (2) of the Bankruptcy (Scotland) Act 1985, an inhibition taken out within 60 days of the effective date of sequestration is of no effect but one taken out prior to this period does operate to give you a preference over other unsecured creditors. Depending on the debtor's property portfolio therefore it may be worthwhile obtaining an inhibition and then waiting 60 days before proceeding to sequestrate.

The second diligence I wish to mention is arrestment which is similar to garnishee. Changes have been made to this procedure by the Bankruptcy and Diligence (Scotland) Act 2008 which make it more creditor friendly. If you lodge an arrestment in the head office of a bank it is up to the bank to determine whether the debtor has an account and the banks will now tell you if your arrestment has been successful and how much has been caught. It is also now possible to arrest cash – useful if the debtor operates a cash business such as a shop, pub or nightclub. Funds arrested are automatically released to the creditor 14 weeks after grant of final decree in a case but can be released earlier by obtaining a mandate signed by the debtor. Again arrestments carried out within the 60 days prior to sequestration fall so if you were successful in seizing funds under an arrestment then you should not proceed with, or at the very least postpone your sequestration proceedings.

If you are acting on behalf of a landlord and are pursuing unpaid arrears of rent then normally you will serve a notice of irritancy and then seek irritancy or forfeiture of the lease. This brings the lease to an end and is normally coupled with an action of ejection to allow you to obtain vacant possession of the premises. Whilst the tenant

remains liable for future rent until the property is re-let please note that the doctrine of privity of contract does not apply in Scotland and accordingly you are not able to pursue previous tenants who have assigned the lease for any arrears or payments.

An alternative to consider in this situation is landlord's hypothec. This term is derived directly from Roman law and allows a landlord to enter into leased premises and to take a charge over all the goods stored there. It is therefore similar to distraint for rent. Previously you gained a charge even if the goods belonged to 3rd parties but had to constitute and enforce this security by a separate action known as sequestration for rent. It was a little used diligence on the basis that if you exercised it you could become liable to meet the debtors preferential debts. However , substantial changes were made to this by the BAD Act. Since 1st April 2008 it now covers almost all commercial rent arrears (items contained in a dwellinghouse, on agricultural land or in a croft are exempt), is created automatically once rent arrears arise and subsists until those arrears are paid. In terms of S208 it gives the Landlord a right in security in any insolvency situation. If acting for a landlord you may therefore wish to push ahead with insolvency proceedings particularly if the debtor operates a manufacturing business or other operation involving a large amount of stock. Pre-insolvency you may wish to try to obtain an interdict or injunction preventing the tenant from removing the items from the property.

Having looked at the basics of diligence I will now turn to the alternative methods used in Scotland to deal with Debt Management or insolvency. The impact of devolution on bankruptcy can be shown by the fact that we managed to get from the Bankruptcy Act 1913 to the Bankruptcy (Scotland) Act 1985 without troubling the UK legislature in the interim but that since devolution we have had two major Acts and two minor ones on the subject of personal insolvency and repossessions. The justification behind this is that there has been an attempt to provide debtors with more information regarding their options and to encourage them into a debt management solution rather than formal insolvency. This has been achieved by a combination of forcing creditors to send out debt information packs when threatening diligence, putting a large amount of government money into regulated debt management schemes and making it harder for creditors to enforce sanctions where a debt management scheme is in place.

The Debt Arrangement Scheme or DAS was introduced under the Debt Arrangement and Attachment (Scotland) Act 2002. The central website, where a lot of useful information can be obtained is:-

http://www.moneyscotland.gov.uk/das/MoneyScotland/Homepage .

A lot of money was put into this by the government to set up a network of dedicated money advisors – in 2004, the year of launch this was £3.5M rising to £5.5M the following year. Despite this take up was exceptionally low, in the initial year it was rumoured that the number of successful schemes in place was in single figures. This was partially because there was no element of debt forgiveness and interest could continue to run. It has been modified several times since and in 2008-9 there were

908 applicants which is still very low compared to protected 7633 protected trust deeds and 14600 awards of sequestration made in the same period.

The aim is to educate and guide the debtor to debt management . As a result it is compulsory in Scotland if suing for a debt or petitioning for Sequestration to send with the papers a Debt Advice and Information Package, which is a leaflet available from the Accountant In Bankruptcy. The aim is to get the debtor to visit an Approved Money Advisor who can be from the public sector, e.g. Citizens Advice Bureau or the local authority or the private sector e.g. Chartered Accountants. Money Advisors can charge for their advice but most is provided free to the user.

The Money Advisor will produce a Debt Payment Programme ("DPP") and will send this out on a Form 4 for approval by creditors. Once the DPP is applied for notice of this is placed on a public register, the DAS Register, and a moratorium on diligence is put in place. Creditors have 21 days to object to the DPP, failing which they will be deemed to have consented. Even if creditors object the DPP can still go ahead if the Money Advisor thinks it is "fair and Reasonable" following criteria set down by the Accountant in Bankruptcy ("AiB").The minimum monthly payment is 1% of the debt due. The DPP is administered by the Approved Money Advisor and the AiB has a statutory Supervisory role. The debtor makes a single payment to a central payments distributor who collects this and then distributes to the creditors under deduction of a fee (normally 10%). Whilst the DPP is being adhered to no diligence (including bankruptcy proceedings) can be brought against the debtor. When calculating the amount available for a DPP any mortgage or rental payment is ring fenced and is not included.

Once approved any interest or penalty payments due on the debt are frozen and are written off if the DPP is adhered to i.e. the creditor is paid the amount of debt stated on the Form 3 (under deduction of the payment distributors charge). If no payments are made on the DAS for a continuous period of 6 months then the DPP can be revoked and the moratorium on diligence removed. You will note however that the DPP does not incorporate any element of debt forgiveness and this is probably the main reason for the low take up rate. Further consultation on the DAS is proposed by the Scottish Government for this summer.

The second form of debt management is a Trust Deed for Creditors. This is similar to an IVA and again is a debtor initiated procedure. It has a long history of use in Scotland, Sir Walter Scott signed a trust deed in 1826. In terms of this the debtor signs a deed placing his assets into a trust fund for the benefit of his creditors. The Trustee is an IP. Previously the IP had to be domiciled in Scotland but this requirement was abolished from 1st April 2008. One of the previous criticisms of Trust Deeds was that there was no set criteria for the assets that had to be placed in Trust and this was used by unscrupulous debtors to try to protect certain assets from Creditors. However in terms of the reforms introduced by the BAD act now the same assets have to be placed in the trust as in a sequestration . The debtor normally also agrees to pay a contribution from his income for a period of 3 years. In order to prevent creditors from carrying out diligence against the Debtor it is necessary for the Trust Deed to become "protected" in terms of Schedule 5 of the Bankruptcy

(Scotland) Act 1985. A notice of the Trust Deed is sent to all creditors and it is also advertised in the Edinburgh Gazette. Unless within 5 weeks from the date of advertisement a majority in number or one third in value of the creditors have objected (and failing to respond is deemed to constitute consent) then the Trust Deed becomes protected. The IP sends a copy of the Trust Deed to the AiB who must forthwith record it in the Register of Insolvencies and the Trust Deed becomes protected on the date of this recording. Access to the Register of Insolvencies can be obtained from the AiB website at http://roi.aib.gov.uk/ROI/faq.aspx -searches are free but you have to log in and register. Alternatively we have an account set up so you can just give me a call if you want a quick check. Once protected then any creditor who has not acceded to the Trust Deed has no higher right to recover his debt than a creditor who has acceded and for all practical purposes this conjoins them to the Trust Deed.

The Trustee thereafter acts in a similar manner to a Trustee in bankruptcy, - he ingathers and realises assets including if necessary the debtors dwellinghouse and thereafter distribute this by way of a dividend to creditors. However please note that there is a specific provision in the Home Owner and Debtor Protection (Scotland) Act 2010 which provides that a domestic dwellinghouse can be excluded from a Protected Trust Deed provided that the debtor arranges with the secured creditor prior to signing the Trust Deed that the secured creditor will not claim in the Trust Deed. Whilst the Act received Royal Assent on 16th March 2010 this section has not yet been brought into force. Assuming it is it is then it could be used by debtors to protect a substantial amount of free equity in the property. The law of unintended consequences will apply here and I think that creditors will press more quickly for sequestration (where this exemption does not apply) in order to increase the pot available. The BAD Act has fixed the accounting period for a Trust Deed as annually so you are going to have to wait at least a year to see some money, the good news is that, on average, Trust Deed Dividends are higher than those in sequestrations. As previously this was effectively the free market rather than state sponsored route to personal insolvency it was lightly regulated and this aspect came in for some criticism, particularly in relation to the fees charged. However under the BAD Act the AiB now has a formal supervisory role in relation to Trust Deeds and can investigate if the actual outcome is substantially lower than that projected in the original statement to creditors. Fees have also taken a hit, just recently Invocas, who were previously the leading supplier of Trust Deeds in the Scottish market have announced their intention to de-list from the AIM Market, a move at least partially brought on by falling profits.

Finally I would like to take a look at sequestration or bankruptcy which is the creditor led route into insolvency. To initiate the procedure you must send your extract registered Certificate of Money Provisions Order to Sheriff Officers who hold a commission for the Sheriffdom in which your debtor resides. They serve a charge on the debtor which is a formal demand to pay the debt within 7 days. If the charge expires without payment then you can proceed to sequestration provided that you are a “qualifying creditor” i.e. one owed £3000 or more. Two or more creditors can combine to reach this threshold. Expiry of the charge constitutes “apparent insolvency” and you have a period of 4 months within which to lodge your petition

failing which you must serve the charge of new. In preparing your petition the Creditor will have to swear an Oath, When you lodge the petition at the Sheriff Court you must send a copy of it to the AiB together with a fee of £200, which was introduced from 1st April 2010. You also have to inspect the DAS Register and confirm in your petition that you have done this and that the Debtor has not applied for a DPP.

Once the petition is lodged then a hearing date is fixed. You must ensure that the petition is served on the debtor not more than 14 and not less than 6 days before the hearing date. This is quite a tight time window and whilst postal service is competent, the prudent course is to instruct Sheriff Officers to carry this out. An important point regarding the petition is that you can nominate whom you require to act as the Trustee. The default provision, in the absence of any specific nomination is that the AiB will become the Trustee. The matter will either be dealt with in-house or sent our to a selected list of accountancy firms who deal with it on an agency basis. It is important to note that whilst the role of the AiB has expanded significantly , there is no Official Receiver in Scotland and the AiB is not equivalent to the OR. The alternative is to nominate your own IP as the Trustee. The good news is that a privately appointed IP will normally do a more thorough job and would therefore be my preferred route if I thought there were either assets to be realised or I wished the debtors conduct to be thoroughly scrutinised. The bad news is that if you take this route then the petitioning creditor underwrites the IP's fees in the event of their being insufficient assets as opposed to the State picking these up if the AiB is appointed. However I have contacts with several IP's who, provided they can get some reassurance that there are realisable assets (normally we carry out a search against the property to check the level of free equity) will agree to limit any fee to the assets recovered.

Previously at the sequestration hearing it was mandatory for the Sheriff to award sequestration unless the debtor could either pay or find sufficient security for the sums due. The sufficient security test was a very hard one and there was criticism that people were not being given sufficient time to re-organise their finances in the face of sequestration. Accordingly this was amended by the BAD Act and it is now possible for the Sheriff to adjourn the hearing if he thinks that the debtor will repay the debt within a period of 6 weeks or will use this period to apply for a DPP.

Once sequestration is awarded then changes in the BAD Act have brought the system very much into line with that practised in England and Wales . The period of sequestration is for 1 year. It was noted in a Scottish Government consultation period that to keep the period at its previous level of 3 years could lead to jurisdiction shopping. Income payment orders or agreements are normally sought and these last for a period of 3 years. Discharge after one year is automatic unless the debtor has failed to co-operate with the Trustee, who submits a report on the Bankrupt's conduct to the AiB. The AiB can seek a Bankruptcy Restriction Order in respect of the conduct and the debtor can also give a Bankruptcy Restriction Undertaking to avoid the court process.

One large change that has been made by the BAD act is in relation to Debtor petitions. These have been removed from the scope of the courts altogether and are now handled as an administrative process by the AiB. Provided he has not been made bankrupt within the previous five years a debtor can petition for his own sequestration if he owes debts totalling £1500 or more (i.e. half the creditor's petition limit). He needs either the consent of a concurring creditor or to have been rendered apparently insolvent e.g. by the service of a charge. He must complete the relevant application forms 9 and 12 which can be downloaded on line from the AiB website. These are effectively a statement of assets and liabilities. Once completed the forms, together with a fee payment of £100 (which ironically cannot be waived) are sent to the Debtor Applications Team at the AiB Office in Kilwinning. They aim to process the application and to award bankruptcy (which is recorded in the Register of Inhibitions) within 5 working days. A specific subset of this is LILA or Low asset Low Income cases. A LILA case is one where the Debtors weekly income is equivalent to the national minimum wage of £232 per week and the Debtor owns total assets of less than £10,000 and no single asset worth more than £1000. The Debtor should also not own any land or a house. Normal social security payments such as Income Support or Jobseekers allowance are excluded from the income calculation. In these cases sequestration is awarded without having to either show apparent insolvency or a requirement to have a concurring creditor. When sequestration in a LILA case is awarded then an advert is placed in the Edinburgh Gazette confirming that a LILA award has been made, inviting creditors to submit claims but confirming that there will be no dividend. Applications for LILA awards are checked by way of audit purposes and 10% of applications are subject to the audit. There are provisions in the Home Owner and Debtor Protection (Scotland) Act 2010 to simplify this further - the Debtor will no longer require the consent of a creditor but instead can obtain a "Certificate of Insolvency" from an authorised person confirming that they are unable to pay their debts. With this Certificate they can apply for their own insolvency. Again this provision has not yet been brought into force and we will need to see what its impact will be on the insolvency scene.

I thought I'd finish by giving you a snapshot of the current scene from the most recent statistics available which are for the last quarter of 2009 and which show:-

3142 awards of Bankruptcy
- 2483 Debtor petitions of which 1905 were LILA cases
- 659 Creditor or Trust Deed conversion petitions

2033 Protected Trust Deeds made

417 Debt Payment Programmes approved.

I hope this has given you a brief overview of Scottish Recovery and Insolvency solutions together with a flavour of what the Scottish market is like but I will be happy to answer any further questions either today or over the phone if you want a more detailed chat.