Scottish Law Commission

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REPORT ON DILIGENCE AND DEBTOR PROTECTION

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SCOTTISH LAW COMMISSION

Items 8 and 6 of the Second Programme

REPORT ON DILIGENCE AND DEBTOR PROTECTION

To: The Right Honourable the Lord Cameron of Lochbroom, Q.C.,
Her Majesty's Advocate

We have the honour to submit our Report on Diligence and Debtor Protection.

(*Signed*) PETER MAXWELL, *Chairman*
R. D. D. BERTRAM
E. M. CLIVE
JOHN MURRAY
GORDON NICHOLSON

R. EADIE, *Secretary*
14 June 1985

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Report of the Commission on the Bankruptcy Laws of the United States, Part I (Washington D.C., July 1973).

CHAPTER 1

INTRODUCTION

1.1 This is the first and main report to be submitted in pursuance of Item No. 8 of our Second Programme of Law Reform,[1] the reform of the law of Diligence.[2] In this report we are concerned with reform of the diligences most commonly used to enforce debts, namely poinding and sale and arrestment of earnings, and also with proposed new orders by which the courts would exercise discretionary control over the enforcement of debts by diligence. One of these new forms of discretionary control is a procedure to be called a debt arrangement scheme, which will be both a method of protecting debtors from diligence and an insolvency process. This report is therefore also submitted in pursuance of Item No. 6 of our Second Programme of Law Reform,[3] which item covers among other things personal insolvency, and is the second report to be so submitted.[4]

1.2 On 23 October 1980, we published the following five detailed consultative memoranda on the topics covered by this report, namely:

Consultative Memorandum No. 47: General Issues and Introduction;
Consultative Memorandum No. 48: Poindings and Warrant Sales;
Consultative Memorandum No. 49: Arrestment and Judicial Transfer of Earnings;
Consultative Memorandum No. 50: Debt Arrangement Schemes;
Consultative Memorandum No. 51: Administration of Diligence;

These memoranda were issued to a wide range of organisations and individuals. We received comments and criticisms on our provisional proposals over the ensuing two years from many persons and bodies, a list of whom appears in Appendix C to this report.

1.3 In preparing this series of Consultative Memoranda, we were greatly assisted by a programme of empirical research on the nature, scale and social aspects of diligence and debt recovery, which was planned by the Central Research Unit of the Scottish Office. The results of this research were embodied in eight reports. At about the same time as our Consultative Memoranda were issued these research reports were published, and were circulated or made available to those whom we consulted as well as to the wider public of those interested in debt recovery in Scotland. The scope of these reports is summarised in Appendix D to this report.

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[1]Scot. Law Com. No. 8 (1968).

[2]*Ibid.*, p. 6. "Diligence" is the legal term used to denote primarily the methods of enforcing unpaid debts due under decrees of the Scottish courts.

[3]Scot. Law Com. No. 8 (1968), p. 5.

[4]Our first report under Item 6 was our Report on *Bankruptcy and Related Aspects of Insolvency and Liquidation*, Scot. Law Com. No. 68 (1982), which is being implemented with modifications by the Bankruptcy (Scotland) Bill presently before Parliament.

Scope and arrangement of this report

1.4 In Chapter 2 of this report, we describe the existing system of diligence and debt recovery; we discuss the aims of reform and the main policy options for achieving these aims, including options put to us on consultation; and thereafter we summarise the main features of our proposals for reform. The ensuing chapters present recommendations in detail for the introduction of a system of "time to pay decrees" in court actions (in effect much enlarging the powers of the court to grant decrees for payment of debts by instalments, which are presently only available in sheriff court summary cause actions);[1] "time to pay orders" after decree constituting the debt has been granted;[2] debt arrangement schemes for the regular and orderly payment in whole, or by way of composition, of debts due by an individual with several debts ("a multiple debtor");[3] wide-ranging reforms of the diligence of poinding and warrant sale;[4] replacement of the existing diligence of arrestment and furthcoming of earnings in the hands of the debtor's employer by three new forms of continuous diligence against earnings, namely, "earnings arrestments" enforcing debts already due, "current maintenance arrestments" enforcing future maintenance (i.e. aliment and periodical allowance on divorce), and "conjoined arrestment orders" enforcing debts due to two or more creditors;[5] reforms relating to diligence enforcing rates, taxes and Crown debts including diligence under summary warrants for the recovery of rates and taxes;[6] reform of the organisation of messengers-at-arms and sheriff officers;[7] and a number of miscellaneous reforms designed to rationalise and modernise various aspects of the law on diligence.[8] Our main recommendations are embodied in a draft Bill which, with notes on clauses, forms Appendix A to this report and are summarised in Appendix B.

1.5 We believe that the reforms mentioned in the foregoing paragraph will enable most debtors who are unable rather than unwilling to pay a debt to obtain time to pay free from the immediate threat of diligence; in cases to which debt arrangement schemes apply, a multiple debtor may obtain a discharge outside sequestration on payment of a composition in accordance with the scheme; and in cases where poindings or arrestments of earnings unfortunately become necessary, these diligences will—it is thought—operate in a manner which, so far as practicable, would avoid undue hardship. These reforms are designed to meet the main criticisms which have been made in recent years of the operation of diligence against debtors, especially poindings and warrant sales. The reforms of arrestment of earnings are designed to make the procedure more effective and less cumbersome for creditors while at the same time not being unduly harsh on debtors.

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[1]Chapter 3.
[2]*Idem.*
[3]Chapter 4.
[4]Chapter 5.
[5]Chapter 6.
[6]Chapter 7.
[7]Chapter 8.
[8]Chapter 9.

Other diligence topics: collection and enforcement of periodical allowance on divorce and aliment

1.6 One topic which has traditionally been considered along with diligence is the machinery for the collection of periodical allowance on divorce and aliment. In this context, in the recent past, the concern has been not so much to protect default debtors but rather to assist a particular class of creditor, namely wives and unmarried mothers seeking to enforce decrees awarding aliment for themselves or their children, and ex-wives seeking to enforce periodical allowance for themselves and aliment for children after divorce. The problem of the collection of alimentary debt has been considered by a number of official reports which have argued the case for introducing official arrangements for the collection of private law maintenance debts in Scotland.[1] It was at one time our intention to issue a consultative memorandum on the collection and enforcement of periodical allowance and aliment,[2] which would have reconsidered the system of collecting officers proposed by the McKechnie Report in 1958 in the light of criticisms made of the English system of magistrates' court collecting officers by the Finer Report in 1974 and other developments.

1.7 As mentioned in paragraph 1.4 above, however, we recommend later in this report the introduction of a new form of diligence against earnings whereby current maintenance (aliment and periodical allowance) would be deducted and paid from earnings by the maintenance debtor's employer. This new form of diligence, called a current maintenance arrestment, is designed to recover so far as practicable maintenance as it falls due and thereby to prevent the accumulation of arrears of maintenance. If successful, it would meet the most serious criticisms of the present law in this area which are concerned more with the difficulties of *enforcement* against an unwilling debtor than with the difficulties of *collection* from a willing debtor. We therefore do not intend to issue a consultative memorandum on collection and enforcement of periodical allowance and aliment unless perhaps our proposals on current maintenance arrestments are rejected.

Other diligence topics: miscellaneous

1.8 In our Consultative Memorandum No. 47,[3] we drew attention to a number of other topics in the field of diligence which may require examination in due course with a view to reform. These topics include diligence (arrestment and inhibition) on the dependence of court actions; inhibitions; arrestment and sale of ships; sequestration for rent under the landlord's hypothec; decrees ordering specific implement of non-monetary obligations; civil imprisonment; adjudication for debt; and some other topics such as the equalisation of diligences outwith sequestration.[4] Apart from the fact that most of these diligences would be affected by the new discretionary orders for the control of diligence, these topics fall generally outwith the scope of our present enquiry, although we have found it convenient to deal with a few relatively

[1]Report of the Royal Commission on *Marriage and Divorce 1951–55* (1956) Cmd. 9678, paras. 980–984; McKechnie Report, paras. 258–298; Grant Report, para. 642.

[2]See our Annual Report for 1977–78 (Scot. Law Com. No. 55), para. 36, at head (5).

[3]*First Memorandum on Diligence: General Issues and Introduction*, paras. 5.6 to 5.19.

[4]Another topic identified at para. 3.40 below as requiring review in due course is the heritable creditor's diligence of poinding of the ground.

minor aspects in this report, including the abolition of civil imprisonment for non-payment of tax penalties and rates.

Acknowledgments

1.9 We are indebted to a large number of persons who have assisted in the work leading up to the submission of this report. Prior to our assumption in 1977 of direct responsibility for preparing consultative memoranda on diligence,[1] a Working Party had undertaken much work on the topic of diligence on our behalf. We would express our gratitude to the members of the Working Party and to those who submitted comments to them. After we had taken over responsibility for preparing the memoranda and reports, we continued to consult individual members of the former Working Party on particular problems. We benefited greatly from the expert advice of Mr. John G. Gray, S.S.C. and the late Mr. James Donald, Messenger-at-Arms and Sheriff Officer. We are especially grateful to Mr. John M. Bell, Messenger-at-Arms and Sheriff Officer, not only for the advice he furnished on particular topics but also for the help which he unstintedly gave to the Central Research Unit of the Scottish Office in preparing and implementing its programme of research into the nature, scale and social aspects of diligence.

1.10 We would express our thanks to the authors of the eight research reports on diligence and debt recovery—Mrs. Barbara Doig, Mrs. Anne Connor and Mrs. Ann R. Millar of the Central Research Unit of the Scottish Office; Mr. Michael Adler and Mr. Edward Wozniak of the Department of Social Administration, University of Edinburgh; and Mrs. Janet Gregory and Mrs. Janet Monk of the Social Survey Division of the Office of Population Censuses and Surveys.[2] We are particularly grateful to Mrs. Barbara Doig who not only researched and wrote three of the research reports (one as co-author), but also planned the whole research programme, organised and supervised its speedy implementation and provided assistance to us in countless ways. Her contribution has been indispensable.

1.11 We are grateful to the Society of Messengers-at-Arms and Sheriff Officers, both office-bearers and individual members, for the statistical and other information which they provided to the Commission and for the assistance and advice which they gave to the researchers on our behalf. Without their help and co-operation, many of the research projects on diligence could not have been implemented.

1.12 We are greatly indebted to Miss Anne Burns and Mr. Derek Fowler, past and present Chief Enforcement Officers of the Enforcement of Judgments Office, Northern Ireland, for their kind assistance in explaining to us the practical operation of that Office.

1.13 Finally our thanks are due to those bodies and individuals who commented on our consultative memoranda,[3] often in long, detailed and carefully considered submissions.

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[1]Twelfth Annual Report for 1976–77 (Scot. Law Com. No. 47), paras. 35 and 36.
[2]See Appendix D.
[3]See Appendix C.

1.14 We wish, however, to make it clear that none of those who assisted us bears any responsibility for any statements not directly attributed to him or her or for the formulation of the policy recommendations contained in this report.

References and abbreviations

1.15 We have sought to take account of two Bills presently before Parliament. References in the text of this report to the Bankruptcy (Scotland) Bill 1984 are references to the Bill as brought from the House of Lords to the House of Commons, and ordered to be printed, on 18 December 1984.[1] We have ventured to assume that this Government Bill, which has by and large received all-party support, will become law in roughly its present form and that it would be realistic and most convenient for all concerned to frame both the report and the draft Bill in Appendix A on that assumption.[2] References in the text of this report to the Family Law (Scotland) Bill 1984[3] are references to the Bill as amended by the First Scottish Standing Committee and ordered to be printed on 2 May 1985. A table of abbreviations of other sources cited in this report is at page xvii.

[1]House of Commons, Bill 48. At the time of the submission of this report, the Bill was beginning its Committee stage in the House of Commons.

[2]In the draft Bill, references are to the Bankruptcy (Scotland) Act 1985.

[3]House of Commons, Bill 140. This Bill is not referred to in the text of the draft Bill in Appendix A to this report.

CHAPTER 2

THE MAIN POLICY ISSUES

Section A. Preliminary remarks

2.1 In this Chapter we seek to identify the principal questions of policy involved in the reform of the important branches of the law of diligence and debt recovery covered by this report; we discuss, in the light of consultation and the research programme on diligence,[1] the main options for the reform of those branches of the law; and we explain our main recommendations for reform and the reasons underlying them.

2.2 Diligence primarily denotes the procedures by which creditors can enforce unpaid debts in Scotland. Though the term has a wider meaning,[2] we are mainly concerned in this report with the two most commonly used forms of diligence which are available to a creditor once the court has granted a decree for payment of the debt. These are the diligence of poinding (pronounced "pinding") and warrant sale (sometimes called charge, poinding and warrant sale); and the diligence of arrestment, in particular arrestment of earnings.

2.3 Poinding and warrant sale is the procedure whereby moveable goods (but not money) possessed by the debtor can be attached by the creditor but left in the debtor's possession until, under the sheriff's warrant of sale, the goods are sold by public auction or if not sold (because no bids above the values appraised at the poinding are made) delivered to the creditor in satisfaction of the debt. The diligence is carried out by an officer of court (messenger-at-arms or sheriff officer) and some of its procedures are supervised by the sheriff. There are special procedures for poindings under summary warrants for the recovery of rates and taxes; these are carried out by officers of court but are not supervised by the sheriff.

2.4 Arrestment is the procedure by which a creditor can attach, in the hands of a third party, any moveable property belonging to the debtor or any sum of money due by the third party to the debtor. In due course, by a procedure known as an action of furthcoming, the arrested property may be realised by the creditor by public auction, or the arrested sum of money paid to the creditor, in satisfaction of the debt. While the diligence has thus a wide scope, we are only concerned in this report with the reform of arrestments of earnings (and pensions, to which similar considerations apply) partly because, for reasons which we explain below, it is the use of arrestments against earnings which is in most urgent need of reform, partly because arrestments of earnings are in practice the main alternative to poindings and warrant sales, and partly

[1]See Appendix D.

[2]Diligence also includes the procedures used (1) to enforce the performance of non-monetary obligations under court decrees, such as the delivery of goods or removing from land, and (2) to attach, or prevent the alienation of, property (a) where the debtor is insolvent or likely to dispose of it (diligence in security of future or contingent debts) or (b) pending the disposal of an action so that the decree can be satisfied (diligence on the dependence). We are not concerned with the reform of such forms of diligence in this report.

because the issues raised by the reform of arrestments of earnings are different in scale and character from the reform of other arrestments.[1]

2.5 In recent years, the procedures for enforcing the payment of debts have increasingly become the target of criticism in Scotland and indeed in many other countries. At all stages in the debt recovery process, consumer debts are much more numerous than other classes of debt and therefore critical scrutiny has naturally focussed on the diligences by which consumer debts are usually enforced, namely the poinding and warrant sale of moveable goods (most often household goods) and the arrestment of earnings. These diligences, especially poindings and warrant sales, can have a very harsh impact on debtors and their families, not only in their effect on the debtor's financial position but also because they occasion personal strain and distress. Doubts have also been raised by some critics (but not by creditors) about their effectiveness. It has been repeatedly emphasised that debt, and therefore the reform of diligence, raises social problems as much as or more than legal problems. Yet until recently the only commentaries on diligence were to be found in technical and largely out-of-date treatises written primarily for lawyers. The resulting difficulties of planning reform were increased by the fact that diligence is not a separate self-contained activity but the culmination of a protracted process which, in consumer and commercial debt cases, commences with the extension of credit by the creditor to the debtor and the occurrence of default in payment and thereafter proceeds through the three stages of "informal" attempts at collection by the creditor or his agents; the raising of a court action for payment; and finally the enforcement of the court decree by either poinding and warrant sale or arrestment.

2.6 Because of the position which diligence occupies in the wider context of the system of debt recovery as a whole, any extensive reform of the main diligences examined in this report can have important repercussions on the earlier stages of debt recovery and conceivably on the granting of credit. Conversely, reforms of the earlier stages of debt recovery can have implications for planning reforms of diligence by, for example, making such reforms less necessary. Before proceeding, therefore, to discuss the defects in the system of diligence and the options for reform, we think it might be helpful to give a short factual description of the main features of the debt recovery system as a whole, using the results of the recent reports on the nature and scale of diligence commissioned by us.[2]

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[1]Arrestments of moveable goods and funds other than earnings work reasonably well, and the main problems concern competitions between arrestments and other diligences and rights (such as floating charges). Arrestments on the dependence of a court action cannot be used against earnings and the reform of that diligence is best treated in conjunction with the reform of inhibitions on the dependence.

[2]See Appendix D. The empirical research for these reports was largely conducted in 1978 and published at about the same time as our consultative memoranda in 1980 so that the comments thereon could be as informed as possible. Where practicable, we give more up-to-date information, and identify subsequent changes in the law. We think, however, that the broad picture which emerged from the research has not significantly changed since 1978.

Section B. Diligence and the system of debt recovery

Types of debt

2.7 Debts can be classified in various ways, and many refinements are possible, but the following classification may illustrate the relevant distinctions. The debt or obligation to pay a sum of money may:

(*a*) arise from the debtor's consent, viz. from a contract or agreement to pay (or less commonly a unilateral bond or promise) or from a failure to pay a sum due under a contract or promise; or

(*b*) be imposed by (i) operation of law such as a statute (e.g. imposing liability for rates or taxes) or (ii) a decree of court (e.g. imposing an obligation to pay periodical allowance on divorce, or transforming the "natural" obligation to aliment a spouse or children into an obligation to pay pecuniary aliment); or

(*c*) arise from some act or failure of the debtor, which amounts to a delict or civil wrong (such as personal injury or damage to property) giving rise to a claim for damages.

As this classification (which is not exhaustive) shows, debts have many different sources. Most debts fall within the first category and arise from contracts involving the extension of credit (e.g. loans and contracts for the supply of commercial or consumer goods and services).

2.8 Credit is an indispensable feature not only of trade and commerce but also of the economy of ordinary families. "Debt" in the broadest sense, is what one person owes another: in that sense, therefore, possibly most adult persons are in debt. A very large number (about half) of Scotland's households live in public sector housing where rent is generally paid one or several weeks in arrear. Most owner-occupiers finance the purchase of their homes by loans repayable over a long period out of income. Gas, electricity and telephone bills are mostly submitted in arrears. There are many different methods of financing the purchase of consumer goods and services, other than an instant cash transaction—e.g. hire purchase, conditional sale, credit sale, charge accounts or budget accounts with the seller, credit cards, vouchers, check trading arrangements and loans from banks, finance companies and other institutions.[1] In principle all these debts may on default be enforced by diligence, though in many cases other means of enforcement (calling up a security, repossession of goods on hire purchase or hire, disconnection of gas, electricity or telephone supplies) are available and may be preferred by the creditor.

Methods of obtaining warrants for diligence

2.9 "Debt" in the narrower and more usual sense, however, denotes "default debt". As a general rule, a default debt cannot be enforced by diligence until the court (Court of Session or sheriff court) has pronounced a decree "constituting" the debt, that is to say, finding that the defender in the action is liable to pay the debt and quantifying the amount payable. An extract (or authenticated copy) of the decree is issued containing a warrant authorising

[1]See e.g. Crowther Report, Part II.

the execution of the diligences of charge and poinding (a separate application for warrant of sale is needed) and of arrestment.

2.10 To this general rule, there are three main exceptions. First, the official collectors of rates and taxes may obtain from the courts, on production of a certificate as to the liability of the rates or tax defaulters, a summary warrant authorising the collector to instruct officers of court to execute diligence without the need for a prior court action.[1]

2.11 Second, certain documents of debt may be enforced by "summary diligence", namely bills of exchange and promissory notes,[2] bonds and contracts registered in the books of court for execution[3] and tribunal awards deemed to be enforceable as if so registered. In such cases, diligence may be executed without the necessity of an action to constitute the debt. The use of summary diligence against consumer debtors seems to be relatively infrequent.

2.12 Third, arrestments of goods and money (other than earnings) in the hands of a third party and inhibitions (prohibiting the sale of heritable property) can be used "on the dependence" of a court action for payment in order to obtain security for the debt. The modes of diligence—poindings and warrant sales and arrestments of earnings—with which we are here concerned cannot be used on the dependence of an action and accordingly the reform of diligence on the dependence is not considered in this report.

The three stages in debt recovery

2.13 We are mainly concerned with the recovery of debts, especially debts due by individuals, by the normal process of court action and diligence, which falls naturally into three stages:

(*a*) the stage at which the creditor or an agent acting on his behalf makes "informal" attempts at collection (referred to here as the pre-action stage);

(*b*) the stage of a court action for payment (referred to here as the court stage); and

(*c*) the stage when the court decree for payment is followed by further attempts at collection or the enforcement of the decree by diligence.

The various steps which may be taken at each of these three stages and the kind of time-scale involved are illustrated by the flow-chart at Figure 1. This shows that the formal stages of sheriff court summary cause proceedings (the most frequently used procedure in debt claims) and enforcement of the decree by diligence are somewhat complicated.

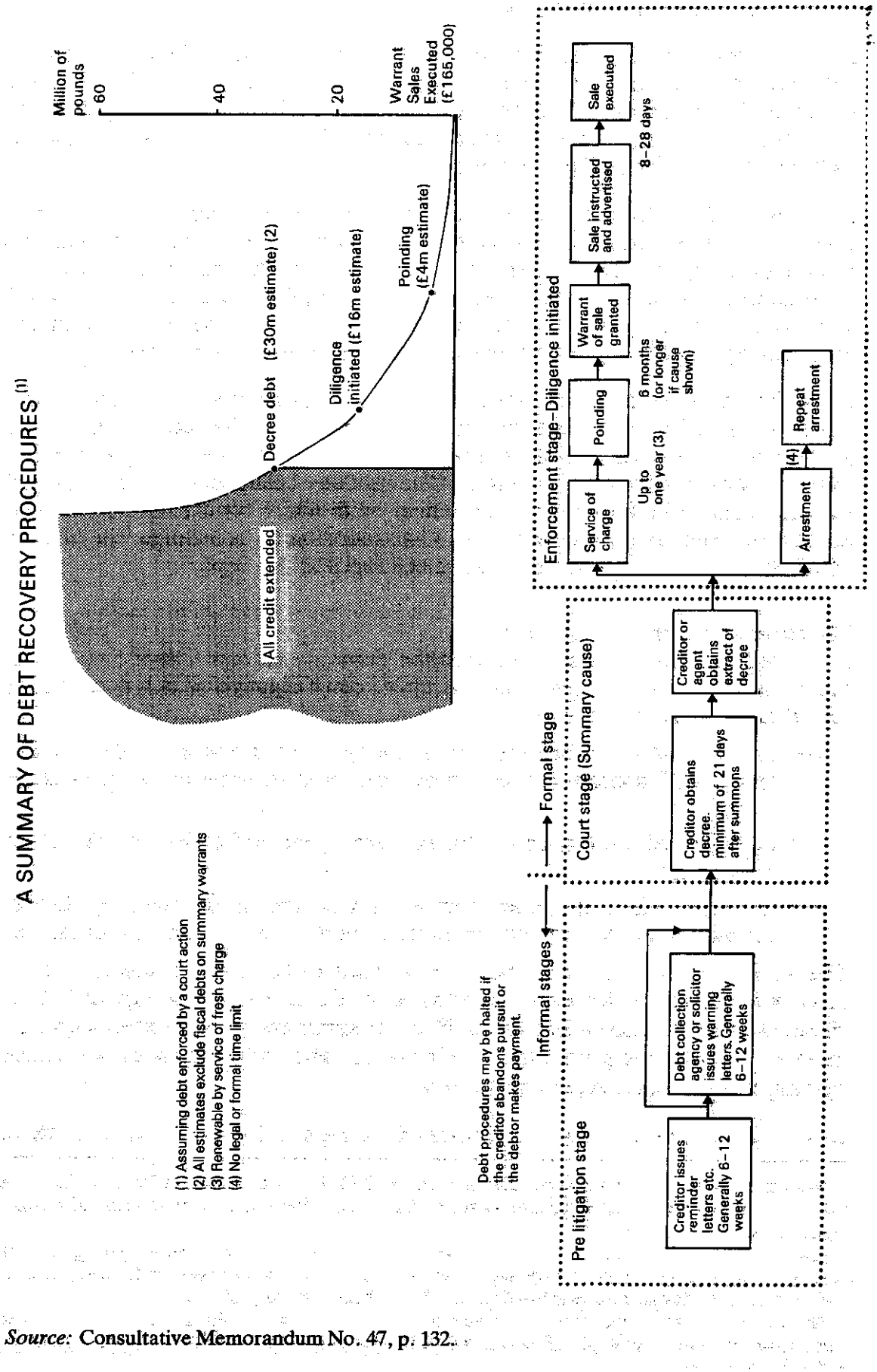
2.14 *The time-scale.* As the flow-chart at Figure 1 illustrates, the whole

[1]Summary warrant diligence is considered at paras. 2.38, 2.168 and Chapter 7 below. Poinding and sale procedures under summary warrants differ from the ordinary procedure of charge, poinding and warrant sale.

[2]Summary diligence is competent where the bill or note is dishonoured by non-acceptance or non-payment and after a procedure known as "protesting" the bill or note and registration of the protest in the Books of Council and Session or the books of a sheriff court.

[3]If such a contract is registered for preservation and execution in the Books of Council and Session or the books of a sheriff court, any sum due under the contract may on default be enforced by diligence.

Figure 1



Source: Consultative Memorandum No. 47, p. 132.

process of debt recovery is protracted. The time-scale varies at different stages. At the pre-action stage it depends on the policies and practices of the creditor, e.g. on the number of communications with the debtor. The C.R.U. Creditors Survey[1] found that there is generally a considerable delay, often as long as nine to twelve months, between the debtor's default and the commencement of a court action. The summary cause action is regulated by a strict time schedule as might be expected in court proceedings: the period involved is a minimum of three weeks until decree and a further two weeks before an extract of the decree is issued. Thereafter, often at least a month elapses before the creditor instructs his agent on enforcement by arrestment or charge and poinding. An arrestment of wages or salary, unless it is repeated, is a "quick" diligence in practice since it only attaches the earnings due at the next pay day and the arrested earnings are normally paid to the creditor then or soon after. By contrast, the diligence of charge, poinding and warrant sale is likely to take at least several months to complete since it is a multi-staged diligence and in most cases each stage is used as a spur to an instalment settlement.

2.15 *The "filter effect" of the debt-recovery process.* At each stage of the debt recovery process, there are fewer cases than at the previous stage. This diminution in numbers results from the settlement of the debt or the creditor's decision to abandon pursuit. Thus, the protracted process of debt recovery acts as a kind of filter so that only a very small proportion of default debts reach the stage of diligence, and in the case of charge, poinding and warrant sale only a tiny fraction reach the final stage of warrant sale. This is illustrated by the graph at Figure 1. The stages of debt recovery are inter-related: the early stages would be ineffective in eliciting payment if the later stages did not exist. If the early stages were ineffective, more cases would proceed to the later stages. This inter-relation between the stages and the filter effect are described more fully in the following paragraphs.

(a) *Pre-action stage: collection by creditor or agent*

2.16 The C.R.U. Creditors Survey yields information on the collection practices of 55 small, medium and large-sized creditor organisations and five debt collection agencies. When default in payment of a debt occurs, the creditor usually pursues its recovery by means of "informal" techniques such as reminders or letters threatening legal proceedings. In the early stages, the creditor normally has an interest in retaining the debtor as a customer and will usually be anxious not to dissipate goodwill, at least until more information becomes available on the nature of the default and the debtor's intentions or ability to pay. Creditors adopt different policies towards the pursuit of default debts: for example, in relation to the amount of debt incurred before positive steps are taken, the "tone" of letters and their frequency. Usually, at least two or three letters are issued commencing with a relatively gently worded reminder and increasing in severity to a letter threatening legal action. The C.R.U. Creditors Survey found that the scale of default which required some form of pursuit varied from 1 in 4 of all accounts to 1 in 10 of all accounts. All creditors said that while their aim was to secure as quick and inexpensive settlement as possible, they wish to retain customers, and they are sympathetic

[1]Paras. 1.10, 4.17 and 4.23.

to debtors' genuine problems, such as bereavement, illness and unemployment. All creditor organisations stressed how difficult it is for them to know the debtor's circumstances, and that the initiative lies with the debtor to inform the creditor of the reasons for default. All creditors said they were prepared to agree to alternative payment arrangements if the debtor was unable to pay at once.[1] After creditors had exhausted their own informal recovery procedures, about three-quarters of them passed over the details of the debt to a debt collection agency or solicitor. Debt collection agencies generally write further letters and also may visit the debtor before deciding whether a court action is worthwhile. The practices of creditors are illustrated by Figure 2.

2.17 These informal recovery procedures result in satisfactory arrangements for payment in the great majority of default debts: systematic, accurate information was lacking but the C.R.U. Creditors Survey estimated that in many organisations the proportion of default debt cases reaching the court stage was less than 1%.[2]

(b) *Court stage: the debt action*

2.18 Where the debtor continues to refuse or delays payment, and the creditor does not write off the debt, the next step is that the creditor raises an action for payment in the Court of Session, or more usually, the sheriff court.

2.19 The main sources of statistical information on this stage are the Civil Judicial Statistics for Scotland, and the C.R.U. Court Survey which studied sheriff court summary cause actions for payment, sheriff court ordinary actions for payment, actions for recovery of possession of heritable property and actions for delivery of goods in 1978.[3] Actions to recover heritable property are usually brought for non-payment of rent, and actions for delivery are usually brought where there has been default in payment of an instalment due under a hire purchase or hire agreement. These are possessory actions rather than debt actions, but usually they arise out of indebtedness. A decree for recovery of possession may be combined with a decree for payment of the debt and usually contains an award of the expenses of the court action which is enforceable by diligence as a debt.

2.20 The majority of debt actions are brought as summary causes, the upper jurisdictional limits of which are £1,000 of principal sum, excluding interest and expenses (£500 in 1978 at the time of the C.R.U. Court Survey). Actions for more than £1,000 are raised as ordinary actions in the sheriff court or in the Court of Session. The numbers of actions in 1978 are described in Table 2.A at page 14.

2.21 *Pursuers and defenders.* The C.R.U. Court Survey illustrates how far consumer debt preponderates in debt actions.[4] In 81% of summary cause payment actions the defenders sued were categorised as "personal" (i.e.

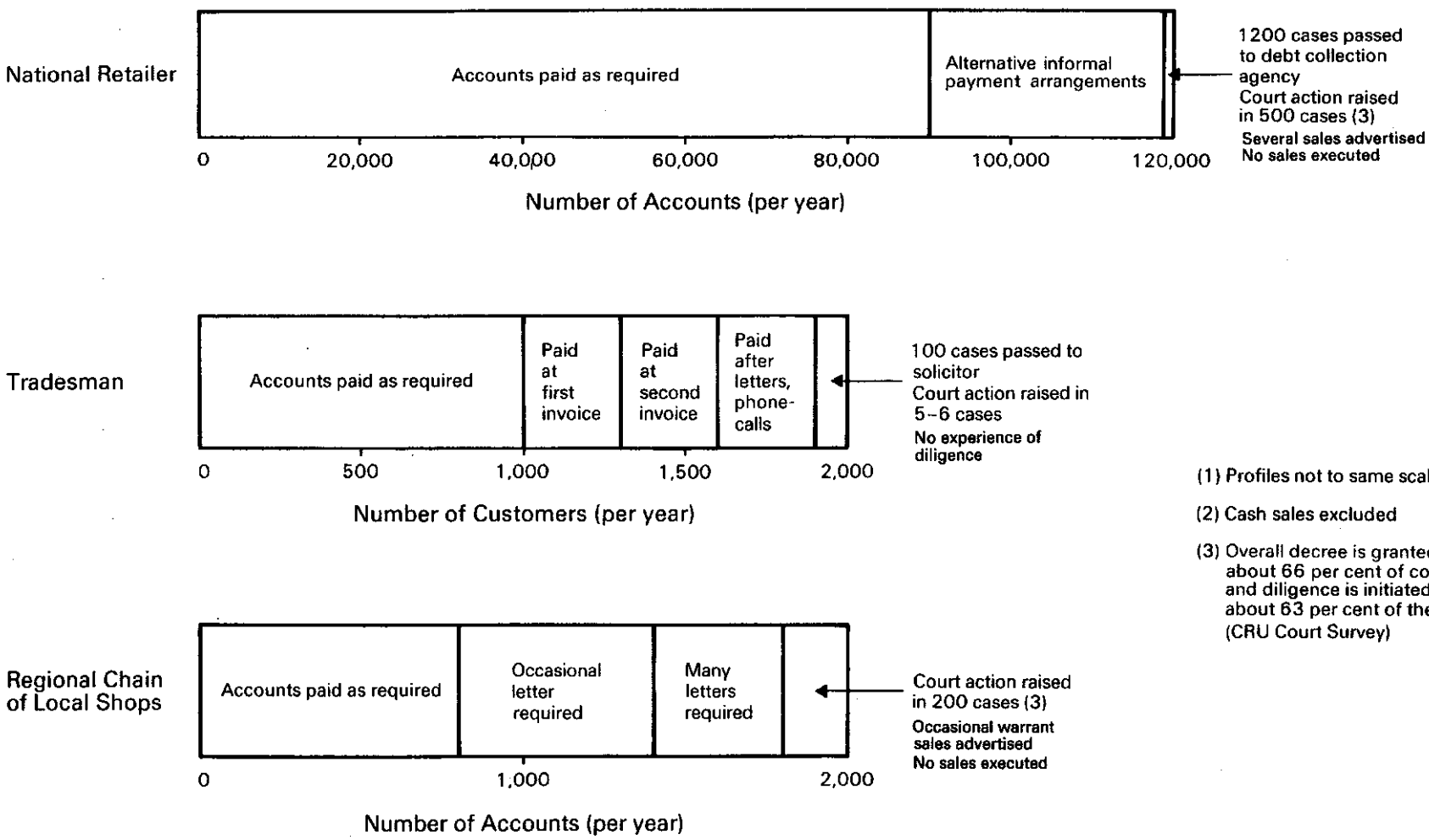
[1]See also C.R.U. Debt Counselling Survey, para. 5.11, which found that creditors "are generally willing to come to informal arrangements with debtors . . .".

[2]C.R.U. Creditors Survey, para. 1.12.

[3]In addition, the O.P.C.S. Defenders Survey gives information on the characteristics of defenders in these "debt-related" actions.

[4]C.R.U. Court Survey, paras. 3.2 to 3.4.

Figure 2 Debt recovery profiles[1] of selected creditors[2]



(1) Profiles not to same scale

(2) Cash sales excluded

(3) Overall decree is granted in about 66 per cent of court cases, and diligence is initiated in about 63 per cent of these cases (CRU Court Survey)

Source: C.R.U. Creditors Survey, Figure 4, p. 44.

TABLE 2.A

DECREES GRANTED IN ACTIONS AND DILIGENCE (POINDINGS AND WARRANT SALES AND ARRESTMENTS) EXECUTED IN 1978

	Total	Court of Session	Sh.Ct. ordinary action	Sh.Ct. summary cause
DECREES IN ACTIONS[1]				
Decrees in favour of pursuer				
Debt decrees	?	?[2]	9,582	72,885
Divorce, other matrimonial decrees and alimentary decrees	9,836	8,794[3]	1,042[4]	—[5]
Other decrees	?	?[2]	1,764	31,490[6]
Total	126,191	9,428	12,388	104,375
(Whereof in absence		698	9,410	100,715
in foro		8,730	2,978	3,660)
Decrees in favour of defender and otherwise disposed of				
Absolvitor, dismissal, sisted, "fallen asleep", remitted[7]	33,355	2,493	6,186	24,676
Total actions disposed of by final judgment	159,546	11,921	18,574	129,051
DILIGENCE[8]				
Decrees passed to officers for enforcement by poinding or arrestment	52,000			
Charge, poinding and warrant sale				
Charges	46,000	700	6,200	39,100
Poindings	20,000	200	2,500	17,300
Warrants of sale	6,200			
Advertisements of sale	3,000			
Sales executed	300			
Arrestments of earnings[9]				
First arrestments	6,000	700	1,300	4,000
Single repeat arrestments[10]	1,700			
Multiple repeat arrestments[10]	1,000			
Total arrestments of earnings	8,700			

Sources: *Civil Judicial Statistics Scotland 1978* (1980, Cmnd. 7762), Tables 3, 4(a) and (b), 6, 9, 10A.
C.R.U. Diligence Survey.

named individuals or married couples) and in 19% were commercial or trading organisations: only 4% of pursuers were "personal". By contrast, in ordinary court payment actions, about one half of the defenders were personal and one half commercial (52% and 48% respectively) and only 8% of pursuers were "personal".[1]

2.22 *Role of debt action.* The purpose of an action for payment is threefold: first, it gives a defender who has a defence an opportunity to dispute liability for the debt or its amount; second, in a summary cause action, it also gives him the opportunity to apply to the court for an instalment decree,[2] and, third, subject to these safeguards for the debtor, it enables the creditor to obtain a decree containing a warrant for enforcement of the debt by diligence. Except when considering whether to grant an instalment decree, the court is not concerned to assess whether the defender can afford to pay what he owes or what the effect will be on him if decree is granted and enforcement proceedings begin.

2.23 The court action itself can have a filter effect since the defender may respond to receipt of the summons by paying the debt. It is estimated that

NOTES TO TABLE 2.A

(1) The statistics include only actions in the narrow sense; they do not include other proceedings disposed of by final judgment in 1978; viz. Court of Session petitions (2,676) and sheriff court applications relating to miscellaneous and administrative business (31,416) among which are 4,934 summary warrants for recovery of rates and taxes. C.J.S. Tables 6 and 12A. In many of these cases, the final judgment may have granted warrant for diligence to enforce an award of the expenses of the proceedings or some other order for payment.

(2) This information is not available from the C.J.S. for 1978.

(3) These include 8,448 divorce decrees many of which contained awards of periodical allowance (6,176 were decrees to wives) or of aliment (in 4,448 divorce actions there were children of the marriage under 16 years of age) but the precise statistics are not available: C.J.S. Tables 4(a) and 4(b).

(4) These include decrees in actions of separation and aliment, adherence and aliment, other actions for aliment, other actions relating to marriage, and affiliation and aliment: C.J.S. Table 10A.

(5) Summary cause decrees of interim aliment are included in the miscellaneous group referred to in note (6).

(6) These decrees comprise recovery of possession of heritable property (27,994), damages (499), sequestration for rent (51), delivery of goods (1,406) and other decrees (1,540) (viz. furthcomings, multiple poindings, interim aliment and specific implement other than delivery): C.J.S., Table 11A.

(7) The great majority of these are decrees of absolvitor or dismissal in the defender's favour with or without an award of expenses enforceable by diligence.

(8) All the statistics on diligence are estimates derived from the C.R.U. Diligence Survey except for the statistics on warrants of sale (6,208) and sales executed (289): C.J.S. Tables 10A and 11A.

(9) The C.R.U. Diligence Survey, para. 3.6 estimates that in 1978 there were 900 arrestments of properties and funds other than earnings (excluding arrestments on the dependence).

(10) A "single repeat" arrestment is an arrestment of the debtor's wage or salary a second time by the same creditor: a "multiple repeat" arrestment is an arrestment against the debtor's wage or salary on a third or subsequent occasion by the same creditor.

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[1]C.R.U. Court Survey, para. 4.13.

[2]See paras. 2.26 and 2.27 below for a description of instalment decrees.

in 1978 about 30% of summary cause payment actions disposed of by the sheriff courts were dismissed, and in the majority of these cases the reason for dismissal was probably that payment arrangements had been made.[1] A further 7% of summary cause payment actions resulted in decrees being granted for expenses only, again suggesting that payment arrangements for the original debt had been made.[2]

2.24 In most cases the debtor admits liability for the debt. Only a very small proportion of cases go to proof (less than 1% [0·9%] of summary cause payment actions), or are continued for several callings (4% of summary cause payment actions continued at first calling)[3] thereby indicating some element of dispute about liability or delay in coming to an arrangement for payment for one reason or another. In 1978, 104,375 summary cause actions of all types were disposed of by decree in the pursuer's favour and of these 100,715 were decrees in absence (viz. undefended) and 3,660 decrees "in foro" (viz. defended).[4] (In 1983, the corresponding numbers were 86,432 of which 84,679 were undefended and 1,753 defended.[5])

2.25 The great majority of actions therefore are largely "administrative" in character. This is shown by the low proportion of defenders who appeared personally or were represented at a court hearing viz. 3% of defenders in summary cause payment actions,[6] and 11% of defenders in ordinary court payment actions.[7]

2.26 In summary cause payment actions, there is a procedure whereby the defender may obtain an instalment decree instead of an "open" decree requiring him to pay the whole debt in one lump sum.[8] The defender may attend court to make oral representations about payment.[9] Alternatively he may make a written offer of instalment payments by notice lodged in court.[10] The notice procedure is much more commonly used since the defender does not have to appear. The notice is in a standard form served on the debtor along with the summons. The pursuer may accept the offer by lodging a written minute in court,[11] but if he does not, the sheriff must consider the offer when the case comes before him.[12]

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[1]C.R.U. Court Survey, para. 3.10 and Table 3 F.

[2]*Idem.* In ordinary court payment actions, only 4% of the actions were dismissed; and in 5% of such actions decree for expenses only was granted: *ibid.*, para. 4.18.

[3]*Ibid.*, para. 3.10.

[4]Table 2.A at page 14 above. A higher proportion of ordinary actions are defended: see that Table.

[5]*Civil Judicial Statistics Scotland 1983*, Table 10 (information supplied by Scottish Courts Administration, pending publication).

[6]C.R.U. Court Survey, para. 3.23.

[7]*Ibid.*, para. 4.19.

[8]Sheriff Courts (Scotland) Act 1971, s. 36(4). If one instalment of such a decree is in arrears at the time when the next instalment falls due, the whole balance due under the decree becomes payable. A decree for payment in a lump sum cannot be changed by the court to an instalment decree, (although in practice the creditor often accepts payment by instalments) and an instalment decree cannot be varied.

[9]Summary Cause Rules, rule 51.

[10]*Ibid.*, rule 52, Form Q.

[11]*Ibid.*, rule 54.

[12]*Ibid.*, rule 55 (as amended).

2.27 It is estimated that offers to pay by instalments are made in summary cause payment actions by approximately one in seven defenders (16%) and in 1978 three-quarters of these were offers of £5 per week or less.[1] Approximately 70% of offers were accepted (and were more often accepted when the offer was over £3 per week and/or when the principal sum was under £50).[2] Overall instalment decrees account for one in five summary cause decrees for payment of money.[3]

(c) *Enforcement stage: the use of diligence*

2.28 After the issue of the extract decree for payment authorising diligence and perhaps following a further letter or letters requesting payment, the next step is that the creditor or his agent (solicitor or debt collection agency) sends the extract decree to the officer of court with instructions to enforce the decree by diligence. Table 2.A at page 14 above shows the numbers of decrees for payment granted in 1978, together with estimates of the number of cases in which diligence was executed. It will be seen that about 126,000 decrees were granted in favour of the pursuer. Of these about 82,000 were sheriff court debt decrees enforceable by diligence (i.e. ordinary action 9,582 plus summary cause, 72,885). An unknown but certainly large proportion of the remaining 44,000 decrees were for payment of sums enforceable by diligence.[4] It is estimated that in 1978, of these decrees about 52,000 decrees were passed to officers of court for enforcement by poinding or arrestment.

(i) *Scale of use of charge, poinding and warrant sale*

2.29 Before a poinding can be executed, the officer of court must serve a charge on the debtor (usually by hand service rather than postal service). The charge requires the debtor to pay the debt, within a specified period (14 days in summary causes), and warns him that, failing payment within that period, his goods may be poinded. It is estimated that in 1978 about 46,000 charges were served as the first step towards poinding and warrant sale. When serving the charge, the sheriff officer may have a chance to assess whether the debtor has poindable goods or may obtain information on the debtor's financial circumstances so that he can report to the creditor on the prospects of recovery. It is estimated that in 1978 20,000 poindings were executed, less than one-half of the number of charges which were served. This numerical decrease is not attributable entirely to payment of the debt: the creditor may decide to write-off the debt on the basis that further steps in the diligence would not elicit payment and that the expenses incurred relative to the amount of the debt would not justify further pursuit. But it appears likely that the service of a charge induces the majority of debtors to make payment arrangements.

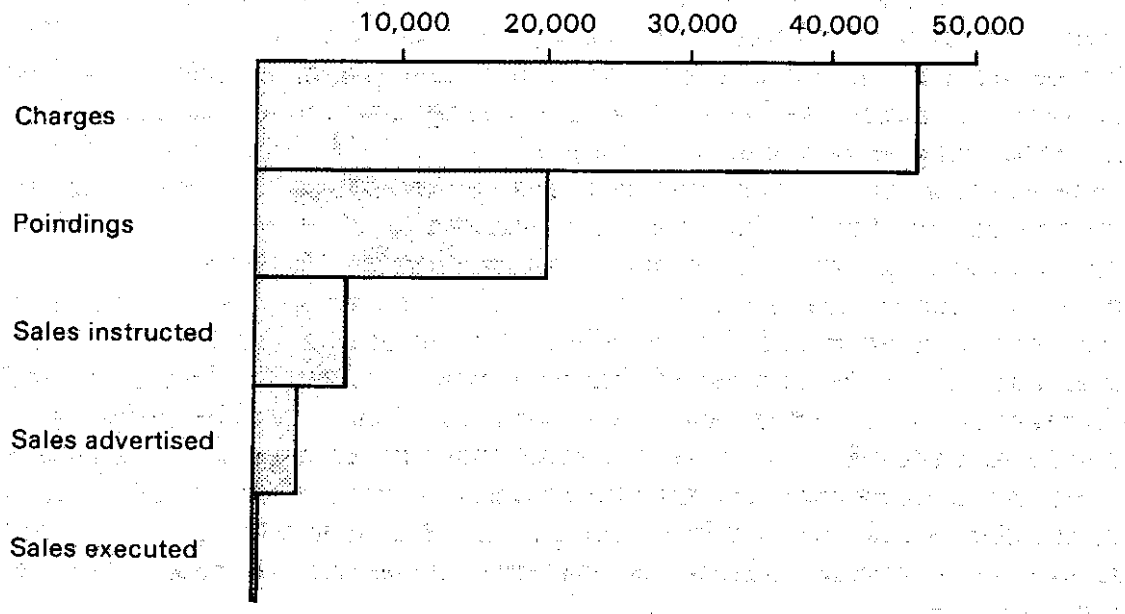
2.30 The warrant in a decree authorises a charge and poinding but not a

[1] C.R.U. Court Survey, paras. 3.27 to 33; para. 6.8.
[2] *Ibid.*, para. 6.9.
[3] *Idem.*
[4] E.g. sums not classified in the statistics as debts such as damages, aliment or periodical allowance on divorce; Court of Session debt decrees; decrees for non-monetary obligations but containing awards of expenses. Statistics for Court of Session debt decrees are only available from 1979: see Table 2.C below.

sale. Accordingly, once the poinding has been executed and reported to the sheriff, the next step is for application to be made to the sheriff for a warrant to sell the poinded goods. This application is not intimated to the debtor who has no opportunity to oppose the application. Until recently the warrant was granted automatically unless it appeared to the sheriff from the report of the poinding that the poinding had not been properly executed. Now the sheriff exercises a limited discretion to refuse warrant of sale.[1] A warrant to sell household goods normally provides for the sale to take place in the debtor's home with the effect that the statutory advertisement of the sale specifies the debtor's name and address. The warrant of sale is intimated to the debtor.

2.31 After a poinding, there is a marked decrease in the number of cases going on to the later stages of diligence as creditors obtain payment or abandon pursuit. Table 2.A shows that of 20,000 poindings in 1978, about 6,000 went on to the stage of grant of warrant of sale, about 3,000 reached the stage of advertisement of the sale and under 300 cases reached the final stage of the sale. This resulting filter effect is graphically illustrated by Figure 3. Published

Figure 3. Charge Poinding and Warrant Sale Procedures 1978



* I.e. cases where warrant of sale granted.

Source: C.R.U. Diligence Survey, Figure 1, p. 8.

[1]See para. 2.60.

statistics of poindings, warrants of sale and sales executed,[1] but not charges or advertisements of sale,[2] are available only from 1979 and are shown at Table 2.B for the period 1979 to 1983. The great majority of sales advertised do not take place either because payment is made or it is not financially worthwhile for it to be carried out. Thus, Table 2.B shows that the proportion of sales executed to poindings has fluctuated being roughly about 1 in 65 (1979); 1 in 91 (1980); 1 in 52 (1981);[3] 1 in 42 (1982); and 1 in 35 (1983), but remains very small. As Table 2.C shows, the proportion of sales executed to debt decrees containing warrant for diligence is even smaller and in the period

TABLE 2.B

POINDING AND WARRANT SALE PROCEDURES: 1979 TO 1983

2.B.1. The total number of poindings, warrants of sale and sales executed: 1979 to 1983

	Poinding	Warrant of sale	Sale executed
1979	14,515	3,838	226
1980	21,096	5,829	231
1981	14,926	4,634	287
1982	17,014	5,195	403
1983	16,478	4,886	477

2.B.2. The number of poindings, warrants of sale and sales executed on summary cause decrees: 1979 to 1983

	Poinding	Warrant of sale	Sale executed
1979	12,881	3,178	145
1980	18,806	4,712	151
1981	12,885	3,565	192
1982	15,168	4,174	282
1983	14,571	3,832	341

2.B.3. The number of poindings, warrants of sale and sales executed on other decrees: 1979 to 1983

	Poinding	Warrant of sale	Sale executed
1979	1,634	660	81
1980	2,290	1,117	80
1981	2,341	1,069	95
1982	1,846	1,021	121
1983	1,907	1,054	136

Source: *Civil Judicial Statistics Scotland,* Tables 3.10. (At the time of submission of this report, the statistics for 1983 had not yet been published and were made available to us by the Scottish Courts Administration.)

[1]I.e. reports of sale whether the goods were actually sold or delivered to the creditor because no bid above the upset price was made.

[2]These are not reported to the court.

[3]It is not clear what the effect of industrial action by court staff in 1981 had on diligence, e.g. by preventing the grant of warrant of sale.

1979 to 1983 has ranged from 1 sale: 170 debt decrees to 1 sale: 365 debt decrees. If account is taken of decrees enforceable by diligence other than debt decrees (the numbers of which are unknown), the proportions are smaller again.

(ii) *Scale of use of arrestments*

2.32 An arrestment only has the effect of bringing the arrested funds (or property) within the control of the court so that the funds cannot be paid (or the property delivered) to the debtor or otherwise disposed of. The arrestee therefore can safely pay (or deliver) the arrested funds (or property) to the arresting creditor only if the debtor authorises him to do so by a written or oral mandate. If, however, the debtor refuses to authorise payment, or the arrestee denies that he has any arrestable liability to account to the debtor, then the arresting creditor must raise an action of furthcoming to require the arrestee to pay him the arrested sum. Arrestment is thus often described as "an inchoate diligence", requiring a furthcoming for its completion. At first sight, therefore, it seems to be exceedingly cumbersome. In practice it is not in the debtor's interest to refuse to authorise the arrestee to pay the arrested funds to the creditor because normally the debtor admits liability for the debt and refusal to release the arrested funds to the creditor would merely render him liable for the much greater expense of an action of furthcoming. For this reason, actions of furthcoming are relatively rare.[1] In short, while in law an inchoate diligence, an arrestment in practice almost invariably operates as a completed diligence, especially when wages or salaries are arrested.

TABLE 2.C

WARRANT SALES EXECUTED AS A PROPORTION OF DEBT DECREES: 1979 TO 1983

	Debt decrees				Sales executed	Sales executed as a proportion of debt decrees
	Court of Session	Sh.Ct. ordinary cause	Sh.Ct. summary cause	Total debt decrees		
1979 ..	541	7,996	60,184	68,721	226	1:304
1980 ..	811	11,560	71,986	84,357	231	1:365
1981 ..	1,203	10,918	59,592	71,713	287	1:250
1982 ..	805	9,675	72,242	82,722	403	1:205
1983 ..	767	11,496	68,679	81,142	477	1:170

Source: *Civil Judicial Statistics Scotland,* Tables 3.10, 5, 9 and 10. (At the time of the submission of this report, the statistics for 1983 had not yet been published and were made available to us by the Scottish Courts Administration.)

[1]The C.R.U. Court Survey identified [Table 2A, footnote (2) at p. 8] 13 actions of furthcoming disposed of in a sample of 5.5% of all actions disposed of in the sheriff courts in 1978: on this basis there may have been 236 actions of furthcoming in the sheriff courts, perhaps 250 in all, in 1978. In 1983, 179 decrees of furthcoming were granted to pursuers (Court of Session 4: sheriff ordinary cause 6; sheriff summary cause 169): information supplied by Scottish Courts Administration pending publication of *Civil Judicial Statistics Scotland 1983*, Tables 5, 9 and 10.

2.33 There are no published annual statistics on the use of arrestments[1] but the C.R.U. Diligence Survey gives uniquely valuable information on the topic. The Survey estimated that in 1978 there were 6,900 first arrestments of wages, salaries or other property or funds of which approximately 6,000 were first arrestments of wages or salaries and 900 were arrestments of other assets such as bank accounts and moveable goods: see Table 2.A. Of the 6,000 first arrestments of wages or salaries nearly 30% were repeated at least once.[2] Normally, a first arrestment will not clear the debt and the debtor will generally make arrangements to pay the balance by instalments over a period.

(iii) *Debtors and creditors involved in diligence*

2.34 The C.R.U. Diligence Survey gives information on the numbers of decrees for payment and other debt-related decrees (viz. for recovery of heritable property and for delivery of moveables) which were passed to officers of court for enforcement in 1978. It is estimated that 90% of such decrees in summary cause actions passed to officers of court for enforcement by poinding, arrestment of earnings, ejection, or recovery of goods were against "personal" defenders (i.e. named individuals or married couples) and only 10% against commercial debtors.[3] This is about the same ratio as for debtors against whom a summary cause decree was pronounced.[4]

2.35 The Survey also shows that the diligence of charge, poinding and warrant sale is most often used against "personal" debtors rather than commercial debtors. About 85% of charges were served against personal debtors and 15% against commercial debtors: at subsequent stages, the ratio fell slightly, except at the stage of advertisement of sale: 77% of warrant sales were against personal debtors.[5]

2.36 Nearly all of the arrestments were against personal debtors (97%) as compared with 85% of the cases in which a charge was served.

2.37 The relative importance of the different types of debt enforced by diligence, is illustrated by the analysis in the C.R.U. Diligence Survey of the pursuer groups involved in enforcing debt-related decrees (viz. payment, possession of heritable property and delivery of goods). The largest pursuer group was commercial organisations (19%) followed by national retailers (11%), finance houses (10%), local authorities (9%), Electricity Boards (9%) and Scottish Gas (6%).[6] Overall local authorities, public utilities and central government departments account for 33% of the decrees enforced by

[1]The courts do not possess information on arrestments because, except in the rare case where an arrestment on the dependence of an action is used prior to the serving of the summons, arrestments are never reported to the court.

[2]The total number of arrestments in execution in 1978 is estimated at about 10,000 made up of 6,000 first arrestments of wages or salaries, 1,700 single repeat arrestments, and 1,000 multiple repeat arrestments (in the survey period from 2–13, the majority being two) and 900 arrestments of property or funds other than earnings. It is thought that there may be about 1,000 arrestments on the dependence every year (estimate based on a survey of 5½-month period in 1974–75 being arrestments of assets other than earnings).

[3]C.R.U. Diligence Survey, para. 5.6.

[4]*Idem.*

[5]*Ibid.*, para 4.1 and Table 1. The ratios were poindings 83 personal: 17 commercial; sale instructed (viz. intimation of warrant of sale) 81:19; sale advertised 84:16; sale executed 77:23.

[6]C.R.U. Diligence Survey, paras. 5.5 and 5.8 and Annex D, Tables 12–14.

"ordinary" diligence.[1] Comparison with the C.R.U. Court Survey discloses that the only pursuer group to show a marked fall in importance between decree granted and diligence stages was local authorities (as a result of the non-enforcement of warrants for ejection); a few pursuer groups (i.e. national retailers, finance houses and mail order firms) instructed relatively more diligence.

Summary warrants for recovery of rates and taxes

2.38 Local rating authorities and the Boards of Inland Revenue and Customs and Excise may obtain from the sheriff court summary warrants for the recovery of rates and taxes without the need for a court action. These warrants are enforced by special poinding procedures which are simpler than the normal procedure of charge, poinding and warrant sale. A charge is not served prior to the poinding and the poinding procedure is not subject to the supervision of the sheriff in the same way as in an ordinary poinding. Rates warrants, but not tax warrants, are enforceable by arrestment.

2.39 Diligence under rates and tax warrants has a similar filter effect to diligence under court decrees. As Table 7.B in Chapter 7 shows, in 1978 summary warrants were granted in respect of almost 5,900 tax defaulters (Inland Revenue 2,127, VAT 3,745) but in the same year only four sales were executed under Inland Revenue warrants and less than 10 sales were executed under VAT warrants. There are no national statistics on rates defaulters but in 1980–81, summary warrants were granted in respect of almost 38,500 rates defaulters in Strathclyde region (containing about half of Scotland's population): as few as seven sales were executed: see Table 7.A in Chapter 7. Lothian exemplifies a similar pattern (*ibid.*).

Section C. The need for reform

The objectives of the system of enforcing debts by diligence

2.40 Our consultation elicited a wide range of different views on the scope and content of the reforms which are needed to the present system of enforcing debts by diligence. While therefore it may be too much to expect unanimity on the precise reforms required, we hope it may be possible to obtain general agreement on the objectives of a good system of enforcement of debt by diligence. We believe that a statement of those objectives, even in very broad terms, is helpful, and indeed necessary, in evaluating the present law and practice.

2.41 We see the general objectives of a good system of enforcing debts by diligence as follows. First, it should seek to provide effective machinery, in which creditors have confidence, whereby creditors can obtain payment of their debts. Second, within the constraints imposed by the need to maintain an effective system of enforcing debts, it should make available procedures which are designed to have proper regard to protecting those debtors who are subjected to diligence from undue economic hardship and personal distress. The extent to which the public have respect for the system depends

[1]To this must be added the rates and tax arrears enforced by summary warrant diligence: see para. 2.38 below.

largely on how far the system attains, and is seen to attain, a proper balance between the twin objectives of effective enforcement and debtor protection.

2.42 It will be seen from the above statement of objectives that we hold to the view that people who are able to pay their legally binding debts should be required to do so. This view was not challenged on consultation and, while there may be divergences of opinion as to what constitutes ability to pay, we believe that this view is generally accepted by public opinion in Scotland. If it were not so, there would be no stigma attached to newspaper advertisements of warrant sales. We are aware, however, that this view is not universally accepted since, for example, arguments have been advanced to the effect that wide classes of consumer debt ought not to be made legally binding at all.[1] These arguments are not considered in this report and were excluded from our consultation for to have admitted them would have required us to review very wide tracts of substantive law (including rules applicable throughout the United Kingdom, e.g. on consumer credit and consumer protection) many of which have only an indirect and even tenuous connection with the law of diligence.

2.43 An important yardstick for measuring the real worth of procedures designed to attain the foregoing objectives is the extent to which the procedures may properly be regarded as cost-effective. Somebody must pay for these procedures, and in the case of most of the procedures, that person can only be the Exchequer, the creditor or the debtor, or some combination of these.[2] Thus, the new or revised diligence procedures and procedures safeguarding debtors from diligence, if they are to be accepted by government and the legislature, must make the best and most economic use of public resources and cause as little expense to creditors and to debtors as is possible consistently with attaining the objectives of the system. Moreover, in the case of arrestments of earnings, the system necessarily places a considerable burden on the debtor's employer who, it may be assumed, bears no responsibility for the debt being incurred or for the debtor's default. Any reform of arrestments of earnings therefore must in fairness also cause as little trouble and expense to employers as is practicable consistently with attaining the objectives of the system.

First objective: effective enforcement

2.44 So far as the first general objective stated above is concerned, it emerged from our consultation and the research commissioned for us that creditors generally regarded the Scottish system of debt recovery and diligence as providing an effective means of recovering debt. Before summarising the evidence on this matter, two preliminary points may be made. First, firm and precise information on the amounts recovered at particular stages of debt recovery and diligence is lacking because creditors' records are (or were at

[1]See e.g. T. G. Ison, *Credit Marketing and Consumer Protection* (1979) who argues (at p. 288) that "debt as a cause of action should be abolished for the price of goods sold at retail".

[2]We are aware that suggestions have been made in the past that the cost of a reformed system of debt enforcement should be borne by a levy on creditors on the model of the Redundancy Fund levy on employers. It is not for us to make proposals on the financing of public expenditure on debt enforcement, but whatever the source of such expenditure, we assume that the need for cost-effectiveness would not be diminished.

the time of the research) generally not arranged by stage in debt recovery or diligence reached but in some other order,[1] and moreover, in the absence of any system of collection by the courts or some other public agency of debts due under decrees, there is no method whereby the recovery of decree debts can be monitored. We have therefore to rely on consultation and the various research reports which yield valuable information on this matter. Second, whether the system of diligence is effective depends to some extent on what criterion of effectiveness is employed, and on this opinions may differ. One approach to this problem is to say that in assessing the effectiveness of the diligence stage of debt recovery, it is necessary to have regard not only to that stage but also to the earlier stages of informal collection by creditors or their agents and to the court action stage. The justification for this is that the earlier stages would be less effective in eliciting payment if the later stages of diligence did not exist as a credible ultimate sanction. Creditors themselves believe that this is a correct approach.[2] Another approach is to look only at the debts which are enforced by poinding and arrestment procedures. On either approach, the evidence is that diligence is effective.

2.45 We have described above the "filter effect" of the debt recovery process whereby, at each stage of that process, fewer cases proceed to the next stage as payment arrangements are made or the creditor abandons pursuit. Only a small fraction (in many businesses under 1% and never more than 10%) of all default debts owed to a creditor proceed to a court action, generally because satisfactory arrangements for payment are made.[3]

2.46 Information on the effectiveness of the court stage in eliciting payment is provided indirectly by the C.R.U. Court Survey and directly by the O.P.C.S. Defenders Survey. The C.R.U. Court Survey[4] points out that the court plays an important constructive role in debt recovery by acting as a channel of, or spur to, communication between the debtor and creditor.

2.47 We referred at paragraphs 2.23 to 2.27 above to the C.R.U. Court Survey statistics of cases which were dismissed or resulted in decree for expenses only, and of cases in which decree was granted but the case was not passed to officers of court for enforcement. The C.R.U. Creditors Survey found that in the great majority of such cases, the reason why the case did not proceed further was that satisfactory payment arrangements were made rather than that the creditor abandoned pursuit and wrote off the debt.

2.48 The O.P.C.S. Defenders Survey found that 84% of defenders in debt or "debt-related" actions arranged to pay all or part of their debt before, during or after the court action: 59% had arranged payment by instalments and 26% outright payment.[5] Debtors who agreed outright payment were in almost every case able to pay off their debt. Of those arranging instalments, just under one quarter (23%) had paid off the debt by the time of the interview (about six months after decree); 59% were still making payments; in 5% of

[1]C.R.U. Creditors Survey, para. 7.5.
[2]C.R.U. Creditors Survey, para. 1.18 and 7.7 to 7.9.
[3]C.R.U. Creditors Survey, para. 1.10.
[4]Paras. 1.7 and 6.12.
[5]*Op. cit.*, p. 47.

cases, D.H.S.S. had taken over the debt; and in only 13% of cases had the debtor defaulted.

2.49 As regards the diligence stage of debt recovery, it is sometimes said that the diligence of poinding and warrant sale is an inefficient mode of debt recovery. This criticism is generally made by persons attacking the system from the standpoint of debtors and concerned to argue that the harsh or potentially harsh impact on debtors cannot be justified on grounds of economic benefit to creditors. The criticism would be justified if the final stage of a warrant sale could be taken in isolation from the earlier stages in the diligence and, indeed, the whole debt recovery process of which it forms part. Thus the C.R.U. Warrant Sales Survey showed that of 285 warrant sales against "personal" or non-business debtors executed in 1977, the sale recovered the relevant debt and legal and diligence expenses in only 3% of such sales.[1] We do not think, however, that the amounts recovered in warrant sales which actually take place provide an accurate measure of the economic efficiency of diligence against moveable goods. That efficiency has to be measured not by reference to the success or otherwise of the final stage in the diligence process, but by reference to the success of the diligence process *as a whole* in eliciting payment of debt in the far greater number of cases which do not proceed to that final stage. As the C.R.U. Creditors Survey[2] observed, any attempt to measure the efficiency of diligence by reference to the level of recovery under warrant sales "can be very misleading because it discounts the role of diligence as part of the wider system of debt recovery and its role as a spur to securing settlements before the final stage of executing a sale is reached".

2.50 The Edinburgh University Debtors Survey gives information on the debtors who made arrangements for payment in response to the stages of poinding and warrant sale from poinding onwards.[3] More than half the debtors entered into arrangements for payment by instalments after each step.[4] The Survey focussed on those who reached the later stages of diligence, in respect of whom payment arrangements had broken down, and does not give a reliable indication on the payments made in the greater number of cases where a charge was served but no poinding followed.[5] On the other hand the instalment arrangements often did not last very long and often went but a small way towards paying off the debt.

2.51 On consultation, only one body representing creditors (the Convention of Scottish Local Authorities) commented to us that the diligence of poinding and warrant sale is inefficient. The Convention represents local authorities which use the special forms of poindings under summary warrants for the recovery of rates (as well as diligence under court decrees). Such information

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[1]C.R.U. Warrant Sales Survey, para. 7. In 57% of sales, all expenses and part of the debt were paid and in 40% of sales only part of the expenses were paid.

[2]Para. 7.9.

[3]*Op. cit.*, paras. 7.42 to 7.44: see also para. 7.8 (charge); paras. 7.22 to 7.25 (intimation of warrant of sale); paras. 7.31 to 7.32 (advertisement of sale).

[4]The proportions were poinding 54%; intimation of warrant of sale 72%; advertisement of sale 60%.

[5]It will be remembered that 46,000 charges were followed by 20,000 poindings in 1978: see Table 2.A at page 14 above.

as we have been able to obtain, however, suggests that poindings under summary warrants for recovery of rates and taxes have a filter effect similar to poindings under court decrees and that the vast majority of rates and tax arrears are recovered without recourse to a warrant sale.[1]

2.52 On consultation, all other bodies representing creditors generally agreed that the diligence of poinding and warrant sale is an effective diligence from the standpoint of creditors. This view was corroborated by the C.R.U. Creditors Survey which observed[2] that the interviews with creditors and debt collection agencies showed that the majority of outstanding debt is paid in response to each stage of the debt recovery process, including the stage of diligence.

2.53 Arrestment of wages is a very effective method of recovery from many points of view. Indeed, a main problem is that an arrestment of earnings is too effective in so far as it leaves the debtor without sufficient funds with which to maintain himself and his dependants.[3] In one important respect, however, arrestments of earnings are not efficient. An arrestment of earnings only attaches earnings due at or before the first pay day following the service of the arrestment; it does not attach earnings due on subsequent pay days. (In cases where earnings are paid in advance, the earnings are not arrestable in the hands of the employer at all unless they are in arrears at the time when the arrestment was laid.) As we have seen,[4] about 30% of arrestments of earnings are followed by further arrestments of earnings. On consultation, there was almost universal agreement with our provisional view that a system of continuous diligence against earnings should be introduced.

2.54 Under the present system, the creditor and not the court instructs an officer of court to execute diligence. The creditor has freedom to decide whether and when to execute arrestments of earnings or other funds or poindings of moveable goods, and he may pursue two or more of these diligences concurrently or consecutively as circumstances when ascertained may require (subject to certain restraints e.g. on second poindings in the same premises which we note below) though normally only one is used at any one time. These characteristics of freedom and flexibility preserve the Scottish system from the kind of criticism which has been levelled[5] at a system requiring creditors to make separate applications to the court for each mode of enforcement and restricting concurrent enforcement.

2.55 The system whereby the creditor, and not the court, instructs an officer of court to execute diligence works well, from the creditor's point of view, because the majority of debt decrees are granted in favour of public utilities, retailers and other commercial organisations who have the necessary resources and information to instruct diligence and do not need the court's help in enforcement. Moreover, creditors who are not corporate bodies can obtain help through the legal aid or legal advice and assistance schemes if the criteria

[1]See paras. 2.38 and 2.39 above.
[2]Para. 7.7.
[3]See e.g. Edinburgh University Debtors Survey, paras. 6.3 *et seq.*
[4]Para. 2.33.
[5]See e.g. Payne Report, para. 295.

of eligibility are satisfied.[1] It is, of course, true that some creditors experience difficulties in enforcing decrees but these are generally difficulties (such as the debtor's insolvency or abscondence) which could not be overcome merely by transferring enforcement functions to the courts.

2.56 So far as we are aware, the main area where creditors are in need of help lies in the collection and enforcement of periodical allowance on divorce and aliment. We have therefore given special consideration to the problems which face such maintenance creditors and make recommendations which would enable them to recover current maintenance out of earnings in order to prevent maintenance arrears from arising.[2]

2.57 To sum up, first, we do not think that the effectiveness of the procedure of poinding and warrant sale can be measured by reference to the very small number of cases in which poinded goods are realised at a warrant sale, because account must be taken of its role, and the role of the court action, in operating as a spur to arrangements for outright payment or payment by instalments. Second, while the proportion of debt paid by such arrangements is not known, it is a substantial amount and is generally regarded as satisfactory by creditors and their agents. Third, the efficiency of diligence against earnings would be improved if a system of continuous diligence against future earnings were introduced.

Second objective: debtor protection

Existing safeguards for debtors

2.58 The achievement of the second objective which we set out above,[3] namely that diligence, though necessarily coercive, should have proper regard to protecting debtors from economic hardship and personal distress, depends at present partly upon immunities from diligence against the person (i.e. civil imprisonment) and upon the exemptions which the law has come to confer upon certain categories of assets and income; partly upon certain restraints on the use of poinding and warrant sale recently evolved by the courts; and partly upon the power of the court to grant instalment decrees in certain classes of case.

2.59 Thus, the common law of Scotland exempted from arrestment against personal earnings sufficient money for the subsistence of the debtor and his

[1]"Legal aid" in the present context denotes representation, on terms provided by the Legal Aid (Scotland) Act 1967 and subordinate legislation, by a solicitor and, so far as necessary by an advocate, in civil proceedings before a court or tribunal, and in taking steps preliminary or incidental to such proceedings. It includes the outlays as well as the fees incurred in such proceedings. Legal aid is available to persons whose disposable annual income or disposable capital do not exceed certain prescribed amounts. The legal aid scheme is supplemented by a statutory scheme providing for legal advice and assistance to be given at public expense under the Legal Advice and Assistance Act 1972 over the whole field of Scots law. Advice covers oral and written advice by a solicitor on any legal problem. Assistance covers negotiations by a solicitor on a client's behalf with a view to settlement of a claim by or against him, but generally stops short of actual representation before a court or tribunal. Eligibility depends on the disposable capital and income falling below prescribed upper limits.

[2]See para. 2.162.

[3]Para. 2.41.

dependants,[1] and it exempted ordinary clothing and tools of trade from poinding or arrestment.[2] These common law principles or rules are nowadays less important than the statutory provisions imposing fixed limits (half the balance above £4 per week) on the arrestment of wages;[3] exempting social security payments from arrestment;[4] exempting certain "necessary" household goods from poinding;[5] abolishing civil imprisonment as a general creditor's diligence[6] and restricting civil imprisonment to cases of wilful default in most of those few categories of debt (aliment, tax penalties and rates) where it remains competent.[7]

2.60 Until recently, it was difficult for an insolvent debtor to free himself from the threat of repeated poindings held over him by a determined creditor (unless the debtor was prepared to take the drastic step of petitioning for his own sequestration under bankruptcy legislation which few consumer debtors do). In recent years, however, some important restrictions on creditors' powers to use the diligence of poinding and warrant sale have been imposed by the courts and by statute including restrictions on the normal duration of poindings,[8] on repeated poindings[9] and on second warrants of sale.[10] Moreover, at one time, a creditor who had poinded goods could pursue his diligence to the final stage of warrant sale even though it was clear that the expenses of the advertisement and sale alone would exceed the proceeds of sale and that expenses would thereby be added to the debt without direct financial benefit to the creditor. Indeed, in small debt poindings, no application for warrant of sale was necessary.[11] With the replacement in 1976 of small debt procedure by summary cause procedure, however, creditors must now in all cases apply to the court for warrant of sale,[12] and the courts have recently developed the law by assuming powers to refuse warrant of sale on equitable grounds, and exercised the powers where the likely proceeds of sale would not cover the expenses of advertisement and sale.[13] These changes have had a considerable

[1]This principle (known as the *beneficium competentiae*) is now in practice only applied in connection with bankruptcy sequestrations, trust deeds for creditors, and "alimentary" liferents, annuities and pensions.

[2]See paras. 5.48 and 5.51.

[3]Wages Arrestment Limitation (Scotland) Act 1870 as amended: the exemption does not apply where the debt enforced by the arrestment is alimentary.

[4]See para. 2.141, footnote 1.

[5]Law Reform (Diligence) (Scotland) Act 1973.

[6]Debtors (Scotland) Act 1880.

[7]Civil Imprisonment (Scotland) Act 1882; Local Government (Scotland) Act 1947, s. 247(5). In the case of tax penalties, civil imprisonment is competent without an application to the sheriff but the procedure is never used in practice. See paras. 7.70 to 7.80 below.

[8]*New Day Furnishing Stores Ltd* v. *Curran* 1974 S.L.T. (Sh.Ct.) 20; Practice Notes of the sheriffs principal have been made limiting directly or indirectly the effective duration of poindings to 6 months. (See Chapter 5 below for a discussion of the cases and Practice Notes referred to in the footnotes to this paragraph.)

[9]*Idem*: the restriction prevents a second poinding (of *any* goods not merely the *same* goods) on the same premises for the same debt unless poindable goods have been brought on to the premises since the first poinding.

[10]*City Bakeries Ltd* v. *S. & S. Snack Bars & Restaurants Ltd.* 1979 S.L.T. (Sh.Ct.) 28.

[11]Small Debt (Scotland) Act 1837, s. 13.

[12]The procedure in poindings and warrant sales on all court decrees, including summary cause decrees, has since 1976 been regulated by the Debtors (Scotland) Act 1838, which formerly applied only to Court of Session and sheriff court ordinary action decrees and summary diligence.

[13]*South of Scotland Electricity Board* v. *Carlyle* 1980 S.L.T. (Sh.Ct.) 98.

impact: in the early 1970s, warrant sales under small debt procedure alone numbered between 931 and 1,861 *per annum*[1] whereas summary cause sales have recently ranged between 341 and 145 *per annum*.[2]

2.61 Another important power available to the court which has the effect of protecting debtors unable to pay from the immediate threat of diligence should also be mentioned. That is the power of the court to order payment of the debt by instalments rather than in one lump sum. This power was originally introduced in 1837 in small debt actions,[3] and when the small debt procedure was replaced by summary cause actions in 1976, a similar power was conferred on the court.[4] This power is subject to two limitations. First, it only applies in summary cause actions i.e. where the principal sum does not exceed £1,000. Second, it cannot be used following the grant of decree so as to convert an "open" decree for payment in a lump sum into a decree for payment by instalments.

2.62 In addition, instalment orders are, or will be, competent in certain special classes of debt. Thus, in relation to sums due under a moneylender's agreement, the court could make an instalment order at any time before payment (even after decree) under the Moneylenders Act 1927.[5] When that Act was replaced by the Consumer Credit Act 1974 on 19 May 1985,[6] the courts were empowered to grant "time orders" providing for payment by instalments of sums due under consumer credit and hire agreements which are "regulated" within the meaning of that Act and under related security agreements.[7]

The impact of diligence on debtors

2.63 The foregoing safeguards for debtors are not inconsiderable, but it appears both from our consultation and the research commissioned by us that debtors subjected to diligence, especially the later stages of poindings and warrant sales, are generally unable rather than unwilling to pay the debt outright and that diligence can have a very harsh impact on debtors and their families not only in their effect on the debtor's financial position, but also because they occasion personal strain and distress.

2.64 *Inability to pay*. The fact that debtors subjected to diligence are generally unable rather than unwilling to pay emerges strongly from the research into debtors' circumstances commissioned for this report. Ability to pay is a complex notion but continuity of employment and level of income are clearly important indexes. The O.P.C.S. Defenders Survey of defenders in debt or debt-related actions[8] found that at the time of the survey (1978), while 5% of

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[1]The small debt sales executed between 1970 and 1975 were 1,431 (1970); 1,861 (1971); 1,175 (1972); 931 (1973); 1,775 (1974) and 1,753 (1975): *Civil Judicial Statistics Scotland* for 1970 to 1975, Tables 11.

[2]Table 2.B.1 at page 19 above.

[3]Small Debt (Scotland) Act 1837, s. 18.

[4]Sheriff Courts (Scotland) Act 1971, s. 36(4); Summary Cause Rules, Form U2.

[5]S. 18(*f*).

[6]Consumer Credit Act 1974 (Commencement No. 8) Order 1983, (S.I. 1983/1551).

[7]Consumer Credit Act 1974, s. 129(2)(*a*): see paras. 3.119 and 4.194 *et seq.* below.

[8]I.e. actions for payment, and summary warrants for recovery of rates, actions for recovery of goods or heritable property.

men in Scotland were unemployed and actively seeking work,[1] among debtors interviewed the proportion unemployed and actively seeking work[1] was as high as 20%; only 45% of debtors interviewed were in full-time employment at the time court action started.[2] It was also found that 41% of debtors were living in households where the main source of income was likely to be state benefits since neither they nor their spouse (if any) were in employment.[3] Nearly half the debtors who were unemployed or temporarily sick had been out of work or away from work for at least six months and over three-quarters for over three months. A clear picture emerged of debtors and their spouses as people on low incomes: over a third of debtors had a weekly income of not more than £30, well below the national average.[4] Ability to pay is clearly also affected by factors such as household size, the number of dependent children and the number of working adults; of particular importance is the relationship between the number of earners and the number of dependent children in the household. Again, debtors were more likely to live in households with dependent children than the population in Scotland generally. Over two-fifths of debtors with three or more dependent children were living in households where neither they nor their spouse were in full-time work.[5] While debtors were typically young (nearly half were aged under 35) married and with dependent children, and were more likely to be in manual occupations (if employed at all) and on a low income, rates debtors (normally pursued by summary warrant) were more likely to be older, in full-time employment and with a higher average income.

2.65 A similar picture of debtors as people on low incomes experiencing difficulty in paying debts emerged from the Edinburgh University Debtors Survey of the impact of diligence on 100 debtors.[6] That survey suggested that debtors subjected to diligence tended to be:

> "young people (mainly in their 30s); they had larger families than the general population, most of their children being of school age. The men were mainly in working class occupations with a particularly large number in unskilled and semi-skilled manual occupations. Unemployment was high and lasted for long periods while household incomes were low; very few wives in families with dependent children went out to work. Although many households were in poor financial circumstances when they took on their debts, many others subsequently experienced loss of employment and/or a drop in income and were in poor financial circumstances when they received the summons."

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[1]I.e. as opposed to retired persons, housewives and others not seeking work.

[2]Section 2.2: Table 2.4. A further 4% were working part-time. The remaining 31% of debtors who were not working included the retired, housewives, or others not seeking work.

[3]This percentage includes cases where the debtors and spouses were (a) unemployed and actively seeking work, or (b) retired persons, housewives, sick or disabled with no job to return to and others not seeking work.

[4]The average weekly earnings in Scotland in 1978 of manual employees over 21 was £81.40 (men) and £50.20 (women) and for non-manual employees was £99.80 (men) and £56.60 (women): *Scottish Abstract of Statistics* No. 10/1981, Table 10.2 (H.M.S.O.).

[5]Section 2.3.

[6]Part 2. For example, a quarter of the sample were unemployed when the credit was extended or debt contracted; over half (58) when the summons was served; and over a third at the time of interview (when a particular step in diligence had just taken place). Para. 2.4.

2.66 The research into debtors' circumstances (which was based on interviews with debtors) found little evidence of deliberate non-payment or delayed payment. The O.P.C.S. Defenders Survey[1] found that only 1% of debtors delayed settlement as a matter of principle; 9% refused to pay the original debt because of some dispute with the creditor; about two-thirds said they got into debt because they simply did not have the means to settle. For 13% the debt resulted from an oversight concerning payment. The Edinburgh University Debtors Survey[2] classifies the main reasons for default given by the 100 debtors interviewed as follows: unable to pay due to loss of income (37) or to increased commitments (16); unwilling to pay (17); marital difficulties (5); able and willing to pay but blamed themselves (8) or a third party (13) or attributed non-payment to misunderstanding with the creditor (4). Since diligence is the last stage in a process which, as we have seen, is very protracted, and gives debtors able to pay ample opportunity to do so, it is scarcely surprising that debtors who are subjected to diligence, particularly the later stages of diligence, are frequently unable rather than unwilling to pay the debt outright.

2.67 *Economic and social impact on debtors.* The Edinburgh University Debtors Survey (which was based on interviews with 100 debtors who had been subjected to arrestment or stages in the diligence of poinding and warrant sale) also provides evidence as to the harsh economic and social impact which these diligences can have on debtors and their families. The impact on debtors of arrestments of earnings and of poindings and warrant sales tend to be different. Arrestments of earnings (which attach half the weekly wages above £4 or, in the case of aliment, rates and taxes, the whole wages) have a more severe impact on the debtor's financial position than poindings and warrant sales. The Edinburgh University Debtors Survey[3] found that the amounts deducted by employers operating wages arrestments were considerably greater than the debtor could reasonably afford to pay: 14 of the 22 debtors' households for which complete information was available had their incomes reduced by arrestment beneath the household's entitlement to supplementary benefit, and of these nine were left with less than 80% of supplementary benefit levels and four with less than 50% of supplementary benefit levels. Most arrestments of earnings (70%) are not repeated and where the arrestment itself does not recover the debt, the arrestment may induce payment arrangements. The Edinburgh University Debtors Survey found that the economic impact of charge, poinding and warrant sale procedures was less than that of arrestments of earnings.[4] As we have seen, the diligence of poinding rarely proceeds to the stage of a warrant sale and the earlier steps in the diligence (the service of a charge, the execution of the poinding, the grant of warrant of sale and its intimation to the debtor, the advertisement of sale) or the threat of the next step, and the threat of the sale itself, are used to spur the debtors to make informal arrangements for payment by instalments out of income. Thus, pressure may be put on a debtor to agree to pay by instalments at a level

[1]Section 4.1.
[2]Paras. 4.1 and 4.2.
[3]Paras. 6.3 and 6.4.
[4]Para. 7.41.

which he cannot meet.[1] In strict law he is liable for the expenses of any new step in diligence executed as a result of his default in payment of the instalments, though in practice if the debtor fails to meet the instalments, the expenses, as well as the balance of the debt, are generally irrecoverable and the creditor abandons pursuit. After decree, as already mentioned, the debtor cannot apply to the court to have the diligence delayed or stopped or for time to pay for example by instalments of amounts which he can pay. Further, in a case where it is uncertain whether the likely proceeds of sale of poinded goods would justify the grant of warrant of sale, a low income debtor may be put under pressure to pay the debt, out of for example social security receipts, by threat of a sale for which the court could not in law competently grant warrant.[2] The debtor must await the creditor's application for warrant of sale and cannot have that threat removed by himself making an application for recall of the poinding.[3]

2.68 The Edinburgh University Debtors Survey concluded that the lesser economic impact of charge, poinding and warrant sale (as compared with wages arrestments) was more than offset by the very considerable social and psychological effects on debtors of poinding and warrant sale procedures, especially the later stages of the diligence.[4] It appears likely that debtors fear and resent newspaper advertisements of warrant sales in their home more than they dislike the sale itself.[5] The survey found that arrestments often had a very substantial adverse effect on the debtor's relationship with his or her spouse, probably due to the loss of income.[6] Poinding and warrant sale tended to have bad effects on the health of the debtor or the debtor's spouse probably due to anxiety associated with the humiliation of the later stages of diligence and this increased as diligence proceeded from poinding to advertisement of the sale (the "high-point" in the process).[7] Other features of the diligence resented by debtors include the execution of a poinding in the presence of friends or relatives of the debtor,[8] and the low valuations placed on household goods by officers when executing a poinding.[9]

2.69 The execution of diligence in inappropriate cases tends to exacerbate the effect of two other problems in diligence, namely diligence expenses and multiple debt.

2.70 *Diligence expenses*. Although the creditor must in the first instance pay the expenses of a debt action to his solicitor and diligence expenses to the officer of court, those expenses are in law recoverable by the creditor from the debtor, so that the burden of the original debt falling on the debtor may be increased by the further burden of the expenses of its enforcement. This burden of expenses may become considerable, whether it is measured by

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[1]See e.g. Edinburgh University Debtors Survey, paras. 7.8, 7.20, 7.23, 7.25, 7.31, 7.43 and 7.44.

[2]Under the test laid down in *S.S.E.B.* v. *Carlyle* 1980 S.L.T. (Sh.Ct.) 98; see para. 2.60 above.

[3]See para. 2.155, head (7) below.

[4]Edinburgh University Debtors Survey, para. 7.41.

[5]*Ibid.*, paras. 7.20, 7.26, 7.28 and 8.6.

[6]*Ibid.*, para. 8.7.

[7]*Ibid.*, paras. 8.8 and 8.9.

[8]*Ibid.*, para. 7.11.

[9]*Ibid.*, paras. 7.14 and 7.15.

reference to the original debt or by reference to the value of the assets against which diligence is done. The amount of expenses involved depends, among other things, on the number of procedural stages through which diligence is required to pass and the most frequently used diligence of poinding and warrant sale has, as we have seen, several such stages. As a result the situation can, and does, arise in which the likely proceeds of sale of the goods to which the creditor has recourse may not only be less than the amount of the debt, but may be less than the aggregate expenses incurred in the diligence.[1]

2.71 *Multiple debt.* Where a debtor is subjected to diligence in respect of one debt, and is simultaneously in arrears with other debts, the execution of diligence may aggravate the problems arising from his multiple indebtedness. Such a "multiple debtor" may enter into arrangements for instalment payments with the creditor who has executed diligence and thereby increase the likelihood of his defaulting in his obligations to his other creditors. Alternatively, he may react passively by taking no action with regard to any of the debts with the consequence that he may ultimately become subject to diligences instructed by his creditors simultaneously. Scots law provides no machinery outside bankruptcy procedures whereby arrangements can be made for the orderly collection and payment of debts due by a multiple debtor to his several creditors.

The primary aim of reform

2.72 Summarising the foregoing analysis, we have concluded that the present system of diligence fulfils its first main objective of effective enforcement and is generally regarded by creditors as satisfactory. The diligence of charge, poinding and warrant sale is an effective method of recovery not as a direct means of realising the debtor's moveable goods in those very few cases which reach the ultimate stage of warrant sale but rather as a sanction inducing payment arrangements in the far greater number of cases which do not go beyond the earlier stages of that diligence and of the debt recovery process as a whole. Arrestments of earnings, which only affect wages or salary payable on one pay day, are effective only because too much is deducted from the debtor's earnings under an arrestment, and it is a considerable disadvantage of the diligence from the creditor's standpoint that it does not attach future earnings.

2.73 On the other hand, it emerged from consultation and the research commissioned by us that the system does not satisfactorily attain the second main objective of protecting debtors who are subjected to diligence from undue economic hardship and personal distress. The evidence suggests that most debtors subjected to diligence are unable rather than unwilling to pay the debt outright out of income or savings and can only pay by instalments. The fear of the later stages of the diligence of charge, poinding and warrant sale, especially the advertisements of sales in the debtors' homes, and other factors including the restricted time-scale of the diligence, induces debtors to agree to arrangements for payment by instalments at a level which they cannot meet. Moreover, diligence expenses increase the debt. Only a restricted use is made of the right to apply for a summary cause instalment decree and there

[1]See para. 2.49 above.

is no other means whereby debtors can obtain an extension of time to pay free from the immediate threat of diligence. Furthermore, arrestments of earnings leave debtors with insufficient funds for the support of themselves and their families. On consultation, it was generally agreed that the primary aim of reform should be to introduce new safeguards protecting debtors subject to or threatened by diligence from undue economic hardship and personal distress.

Section D. Discretionary control of diligence: possible options

2.74 While it was generally agreed on consultation that the primary aim of reform should be to introduce new legal safeguards protecting debtors who are subject to diligence, or the threat of diligence, from undue economic hardship and personal distress, our consultation also revealed that a broad range of different views exists on what form the safeguards should take.

2.75 The possible safeguards which could be employed include powers, conferred on a court or quasi-judicial body, to control enforcement by making orders preventing, restricting, stopping or delaying diligence. The power to make such orders might be supplemented by powers to make orders giving the debtor time to pay a particular debt or debts by instalments or otherwise, or orders making provision for the orderly and regular payment by a multiple debtor of all the debts due to his several creditors. The possible safeguards might include orders (such as are traditionally found only in bankruptcy procedures) which would go beyond the stoppage of diligence or extension of time to pay, and would give an insolvent debtor a discharge of a debt or debts normally on payment of a composition of less than 100p in the pound. Or the safeguards might consist of restrictions on enforcement imposed, not by orders of a court or other body, but by operation of law, such as exemptions of particular categories of property or of categories or levels of income from diligence, or immunity from diligence of particular classes of debtor. Each of these safeguards could take a variety of different forms. Where the safeguards involved discretionary powers conferred on a court or quasi-judicial body, the powers might be introduced at early or late stages of the process of debt recovery. Such powers might be exercisable by the court or other body of its own accord, or on the debtor's application, or in court actions or enforcement proceedings initiated by the creditor. Nearly all of the solutions discussed in our consultative memoranda or proposed to us on consultation involved different combinations or "packages" of these different forms of debtor protection.

2.76 In considering the various policy options, it seems helpful to make a somewhat rough distinction between two broad categories of reforms safeguarding debtors, namely, on the one hand, the introduction or revision of discretionary orders, made by a court or other independent body, authorising diligence or controlling diligence (i.e. preventing, restricting, stopping or delaying it) and, on the other hand, reforms of the manner in which the main diligences of poinding and sale and arrestment of earnings are carried out, of the legal rules on exemptions from those diligences, and of the specific conditions and safeguards built in to these diligences. These two categories of reforms are distinguished for ease of exposition though to some extent they overlap. In this Section and Section E of this Chapter, we consider what kind

of system of discretionary orders authorising or controlling diligence should be available leaving till Section F the question (which is just as important) of the specific reforms required to the diligences of poinding and sale and arrestment of earnings.

2.77 Our consultation revealed widespread support for the introduction of discretionary orders controlling diligence. There was, however, a measure of disagreement on the answers to five important questions of policy, namely:

What body should have jurisdiction in entertaining debt actions and in authorising and controlling diligence—the ordinary courts of law or a body specially created to exercise that jurisdiction?

Should a debtor's disclosure of his means to that body be a compulsory prelude to enforcement or alternatively a condition of a voluntary application by the debtor to that body for the control of diligence?

At what stage in the whole process of debt recovery should orders controlling diligence be available?

What types of order controlling diligence should be available (e.g. orders giving the debtor time to pay by instalments or otherwise; orders providing for the orderly and regular payment of debts due by a multiple debtor; summary bankruptcy procedures; or orders declaring individual debts to be wholly or partly unenforceable)?

What procedural or other reforms are needed to make the orders readily available to those debtors for whom they are designed?

In this Section and Section E we attempt to give reasoned answers to these questions.

2.78 Our research and consultation also suggested that a choice has to be made between the following different types of system, namely:

(1) a system whereby diligence enforcing a debt could not be used unless and until the court, or a newly created special tribunal or arbiter, in an application by the creditor for enforcement by diligence, decided on the basis of an enquiry into the debtor's means that enforcement by diligence was appropriate in the circumstances of the case (see paragraphs 2.79 to 2.110 below);

(2) a system which would allow a creditor to pursue his debt by court action and diligence as under the present law, but would confer on the debtor a new right, exercisable at early or late stages of the debt recovery process, to apply to a special tribunal or arbiter for an order controlling diligence (see paragraphs 2.111 and 2.112 below);

(3) a system whereby, after a charge had been served following on a decree, diligence was replaced by a summary bankruptcy procedure (see paragraphs 2.113 and 2.114 below); and

(4) a system on the lines of that described at head (2) above but with the important modification that the debtor would apply to the court, rather than a special tribunal or arbiter, for an order controlling diligence (see Section E below).

(1) One possible option: enforcement conditional on discretionary authorisation by court or special agency and on prior compulsory means enqury

2.79 Turning to the first of these options, we have considered three different schemes whereby enforcement by diligence would be conditional on discretionary authorisation and a prior means enquiry to which the debtor would be compelled to submit. The first of these is the setting up of a single centralised enforcement agency, called an Enforcement Office, such as has been recommended for England and Wales and established in Northern Ireland, which would authorise and control enforcement after the debt was constituted by a court decree. The second would require that the ordinary courts of law should grant or refuse authorisation of diligence on the basis of a means enquiry in all cases. The third would involve the transfer of jurisdiction in the "constitution" of admitted debts (i.e. debts in which liability was not disputed) from the courts to a body called a debt arbitration service which would also have powers to authorise or refuse to authorise enforcement, on the basis of a means enquiry, of all debts "constituted" in undefended cases by the debt arbitration service and in defended cases by the courts.

(a) *Centralised enforcement office (Payne Report and Enforcement of Judgments Office, Northern Ireland)*

2.80 In our Consultative Memorandum No. 47,[1] we sought views on the possibility that an Enforcement Office should be established in Scotland against the background that similar proposals had been made for England and Wales by the Payne Report,[2] that such an agency already existed in Northern Ireland [3] and in the light of suggestions by the Law Society of Scotland that the concept of an Enforcement Office might merit serious consideration.[4]

2.81 If an Enforcement Office system were to be introduced on the lines described in our Consultative Memorandum, the right to do diligence would cease to be a right available to a creditor, but would become the exclusive right of a new public agency, the Enforcement Office, to whom a creditor would require to apply if he wished to enforce a debt. The Enforcement Office would have both the executive function of carrying out the competent modes of diligence and the judicial function of granting warrant for and controlling diligence. The Office would be staffed by full-time, salaried civil servants of the Scottish Court Service. Certain of the more important orders controlling enforcement would be made by sheriffs attached to the Office and exercising its jurisdiction or "judicial officers" employed within the Office. Where a creditor applied for the enforcement of his debt, the Enforcement Office would decide whether enforcement should be permitted, or whether controls should be imposed on enforcement. Its decision would be made on the basis of a prior enquiry into the means and circumstances of the debtor. In the case of larger debts at least, before the creditor was put to the expense of making an application for enforcement, he would be entitled to apply for a compulsory means enquiry for a smaller fee than that exigible for an application for enforcement. In those cases where the Enforcement Office

[1]Paras. 1.82 to 1.86; Appendix C.

[2]Part III.

[3]Judgments (Enforcement) Act (Northern Ireland) 1969 which, with amending enactments, is now consolidated in the Judgments Enforcement (Northern Ireland) Order 1981 (S.I. 1981/226).

[4]Similar schemes have been recommended in other Commonwealth jurisdictions including Ontario and New Brunswick.

thought that diligence should be restricted or regulated in any way, it would, acting in its judicial capacity, make the appropriate orders controlling enforcement. In those cases where the Enforcement Office thought diligence was appropriate, it would be able to use any available modes of diligence to enforce the debt just as a creditor would at present. An Enforcement Office could also, if desired, be given responsibility for the collection of debts whose enforcement it authorised. The Enforcement of Judgments Office in Northern Ireland acts as a collecting agency in certain cases (e.g. attachment of debts or earnings),[1] and the Payne Committee considered that, if an Enforcement Office were introduced in England and Wales, it might collect debts due under decrees lodged for enforcement to enable the Office to control the course of enforcement and to distribute the proceeds among several judgment creditors.[2]

(b) *Compulsory means enquiry prior to authorisation of diligence by court*

2.82 The requirement of a compulsory means enquiry prior to diligence could be engrafted on to the present system of court action and diligence without establishing an Enforcement Office. In such a scheme, the court would grant decree for payment of a debt or expenses in an action but, in contrast to the present law, the decree would not contain a warrant for diligence. Instead, after obtaining decree, the creditor would be required to make a special application to the court for leave to enforce the decree by diligence. In such an application, the court would decide whether or not to grant leave on the basis of an enquiry into the debtor's means or ability to pay. Examples of means enquiries as a compulsory prelude to a *particular* method of enforcement can be found in other jurisdictions including England and Wales, where such enquiries are a prerequisite of attachment of earnings orders.[3] In the scheme now under consideration, however, a means enquiry would be necessary before *any* method of enforcement was used.[4] There is no exact Scottish precedent.[5] On consultation, a scheme on these lines outlined in our Consultative Memorandum No. 48[6] received some support though it was rejected by the majority of those who commented.

(c) *Debt arbitration service replacing court actions for debt and diligence*

2.83 The concept of a debt arbitration service, which has been developed by the Scottish Council of the Labour Party[7] among others,[8] would involve the

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[1]Judgments Enforcement (Northern Ireland) Order 1981, articles 70(1) and 73(2).

[2]Paras. 416–421.

[3]Attachment of Earnings Act 1971.

[4]Legislation requiring a means enquiry before the use of any method of enforcement has been enacted in the State of South Australia—Enforcement of Judgments Act 1978—but we understand that the legislation has not been brought into operation.

[5]The nearest analogue is the procedure in the Civil Imprisonment (Scotland) Act 1882, s. 4, for imprisonment of alimentary debtors for wilful failure to pay arrears of aliment within the days of charge. The onus is on the debtor to prove that his failure was not wilful. Warrant will not be granted if since default the debtor has not possessed, or been able to earn, the means of paying the arrears, and again the onus of proving this appears to rest on the debtor. There is no question of compelling the debtor to appear for a means enquiry by imposing a fine or an additional period of imprisonment.

[6]Paras. 1.20 to 1.26.

[7]Policy Statement on Warrant Sales presented to the 67th Scottish Conference of the Labour Party, March 1982.

[8]See e.g. Adler and Wozniak, "More and Less Coercive Ways of Settling Debts", *Scottish Government Yearbook 1980*, 161.

creation of a new public service or agency which would assume responsibility not only for the enforcement of debts but also for constituting the debtor's liability to pay undisputed debts. Unlike the two schemes just described, it would therefore affect the court action stage of debt recovery.

2.84 The arguments for such a scheme are based on the premise that the courts as such have no necessary or useful function in relation to undisputed debt. It is argued that in those cases (which constitute the overwhelming majority) where a debtor does not dispute his liability to pay, no need arises for any "adjudication" by a court. What is needed, it is said, is an investigation by an appropriate body into the question of how the debt can best be paid having regard to the individual debtor's circumstances. That body, it is argued, ought not to be the court but should be a new public agency staffed by salaried officials and supplemented by debt counsellors. The function of this "debt arbitration service" would be to assess each individual debtor's circumstances and its arbiters would have the power to make appropriate orders for payment of the debt in the light of that assessment.

2.85 The pursuit and recovery of debts under the proposed system of arbitration would, as we understand it, be likely to work in this way:

(1) Where there was default in payment of a debt and the creditor sought repayment, he would require to approach the debt arbitration service who would contact the debtor and would arrange for one of their debt counsellors to visit the debtor for the purpose of discussing a voluntary arrangement for payment.

(2) That discussion would proceed against the background that unless there was a dispute as to the existence of the debt (in which case the courts would require to be involved), the manner of its payment and the sanctions for non-payment would fall to be determined, failing agreement, by arbitration.[1]

(3) In those cases where the debt counsellor could not obtain a voluntary agreement between debtor and creditor and resort to arbitration became necessary, the arbitration itself would take the form of an informal hearing before an arbiter who would decide, in the light of information disclosed by the debtor and the creditor, on an equitable method of payment. The arbiter would be empowered to make orders for payment by periodic instalments or otherwise; on default, orders for deduction from wages at source; and orders declaring the debt unenforceable or reducing the sum payable. It would appear that poindings and warrant sales would not be permitted, though this is not entirely clear.[1]

(4) In those cases where the debt arbitration service did order debts to be enforced the service would also act as an agency for the collection of the debts in question.

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[1]In the case of a debtor who refused to co-operate in the proceedings, the Statement acknowledged that there is an argument for retaining the summary cause procedure.

Advantages of schemes based on compulsory means enquiries

2.86 There is little doubt that schemes on the lines which we have just described, assuming that they were practicable, would give substantial protection to debtors from the harsh effects of diligence and solve some of the problems of the present system (although, as we mention below, only at the cost of creating or aggravating other problems).

2.87 First, we have seen that creditors are usually willing to accept payment by instalments from debtors in genuine financial difficulties. Unfortunately, debtors who can only pay the debt by instalments or after a breathing space often fail to make contact with the creditor to explain their position and to negotiate payment arrangements. Thus the Scottish Association of Citizens Advice Bureaux (whose bureaux act among other things as debt counselling agencies and as "brokers" for informal payment arrangements[1]) observed to us: "The basic problem in CAB experience is getting the debtor to come forward at an early stage in the debt recovery process to state explicitly the circumstances which prevent timeous repayment of the debt". A procedure for making payment arrangements based on a compulsory means enquiry conducted by an independent body before diligence was begun would, in cases where the debtor submitted to the compulsion, bridge this communication gap. The creditor would be compelled to consider payment arrangements proposed by the debtor or independent body at a stage when, according to the evidence of debt counselling agencies,[2] creditors are more receptive to offers to pay by instalments or requests for time to pay than they are at the later stages of diligence.[3]

2.88 Second, a compulsory means enquiry conducted by an independent body before diligence was begun would enable that body to impose on the parties arrangements for payment by instalments of reasonable amounts and, if these arrangements were successful, both creditors and debtors would be relieved of the burden of diligence expenses. It would also in some cases prevent the execution of unproductive arrestments, charges or poindings.

2.89 Third, a compulsory means enquiry by an indepedent body would often enable that body to select the most appropriate mode of diligence in the circumstances. This may be a considerable benefit given that poindings are quite frequently used, even though the debtor has arrestable earnings, simply because the creditor does not know the name and address of the debtor's employer.

2.90 Fourth, a compulsory means enquiry system would make possible the introduction of a system of attachment of earnings orders, in which the levels of deductions are fixed by reference to the circumstances of the particular debtor, and which has therefore some advantages over a system of earnings arrestments, such as we recommend below, where deduction levels are fixed by legal rules.

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[1]See C.R.U. Debt Counselling Survey, Part 5.

[2]C.R.U. Debt Counselling Survey, para. 5.31.

[3]At the later stages of the diligence of poinding and warrant sale, there are and have to be limits on the duration of the poinding and these restrict the scope for negotiated settlements. We make proposals later for relaxing the time limits on the duration of poindings in order to encourage negotiated settlements of reasonable amounts.

Disadvantages of schemes based on compulsory means enquiries

2.91 Although a system of enforcement conditional on prior compulsory means enquiries would confer significant benefits, it would suffer from formidable disadvantages. The experience in criminal fines cases suggests that a compulsory means enquiry system would present difficult problems.[1] To have even a chance of being accurate, a means enquiry must involve a very complex process and even then a wholly accurate picture may not emerge. As the Scottish Council on Crime observed in relation to fines:

> "Even with time and manpower available for the purpose, it is not easy to establish an individual's means—his capital, income and commitments, necessary and less than necessary. This has, for instance, been the experience of the Supplementary Benefits Commission in assessing disposable income and disposable capital for the purpose of the civil legal aid scheme. The calculation is, by itself, quite complex and it requires exact information of a kind which is available only if the person being assessed will, and can, declare it accurately."[2]

If a complex task of this kind were to be attempted in all cases before enforcement, the price would be considerable delay in the enforcement of diligence in those cases which eventually proceed to diligence. Given that the time scale is protracted anyway, the delay may not matter in many cases, though in other cases it would. There are, however, more serious disadvantages than delay.

2.92 *Relevance of the "filter effect"*. A system making enforcement conditional on a means enquiry in every case where enforcement is sought might be realistic if most of the debt cases in which court actions are raised, or diligence is instructed, reached the harsh later stages of poinding and warrant sale. But in reality, the actual position is very different because of the filter effect on the debt recovery process which we have described above. It follows from this filter effect that the earlier in the debt recovery process a compulsory means enquiry is held, the greater will be the number of inappropriate cases (i.e. of debtors able to pay or not at risk of suffering the later stages of poinding and warrant sale procedures) which will be caught by it. The O.P.C.S. Defenders Survey discloses that most debtors involved in debt and debt-related actions arrange to settle their debt by payment before diligence is commenced and shows how debtors raise the money:[3] of debtors who made payment arrangements, about one-third (36%) made economies; just under one-third (29%) found the money through an improvement in their personal or household circumstances; 19% had always had the money; 18% borrowed money and 5% (4% of all debtors interviewed) ignored other bills.[4] When asked specifically, only 7% reported incurring further debt (apart from money

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[1]The Second Report on *Criminal Procedure* Cmnd. 6218 (1975) (Chairman, The Hon. Lord Thomson) para. 60.16 remarked that of all the topics on which they received evidence, the means enquiry procedure in fines enforcement was subjected to the strongest criticism from their witnesses.

[2]Report on *Fines*, published by Scottish Home and Health Department, (October, 1974) para. 4.19.

[3]Part 8 on "Payment arrangements".

[4]Section 8.6 and Table 8.11. The remaining debtors found the money through a cash gift (5%) sold something (2%); or were unspecific as to how the money was paid (6%); or found the money in other ways (1%).

borrowed to settle the original debt) as a result of having to raise the money to make settlement.[1] This evidence does not suggest that "desperation borrowing" by debtors is widespread at the earlier stages of debt recovery before decree is granted or diligence commenced. Nor does this evidence suggest that a compulsory means enquiry should be held in every case at that stage, though it does suggest that debtors (e.g. those who require to borrow, or do without "essential" goods and services, in order to pay the debt) should have the right and the opportunity to apply for time to pay at the stage of a court action and *a fortiori* when diligence is imminent.

2.93 In our view, to hold a compulsory means enquiry in every case before any diligence has been commenced at all would be an extremely wasteful use of resources. For example, the Enforcement Office and court-based means enquiry solutions envisage that a means enquiry procedure would be held after decree for payment and before diligence was begun. This would mean that means enquiry procedures would be used in all cases in which officers of court were instructed to do diligence by charge, poinding or arrestment, perhaps about 50,000 cases a year (1978 figures). Yet less than half of these proceed to a poinding (20,000 cases in 1978), and less than 1% of such cases result in a warrant sale (300 in 1978).

2.94 The debt arbitration service scheme envisages that its procedures would be used in all cases of debts of up to £5,000. These procedures would usually involve visits by debt counsellors to the debtor in his home or a means enquiry by an arbiter or both. Recent statistics of court business suggest that these elaborate procedures would have to be used in about 110,000 cases a year in lieu of the corresponding number of debt actions.[2] Depending on the scope of the scheme, it might also have to be used in several tens of thousands of rates and tax arrears cases presently dealt with under summary warrant,[3] and, if rent arrears cases were included, a very large proportion of the present number of actions to recover heritable property.[4] This might entail a total of over 150,000 cases dealt with by debt counselling or means enquiry procedures.

2.95 It seems to us therefore that these solutions would dissipate public financial and manpower resources which might otherwise be concentrated on assisting the very much smaller number of debtors for whom protracted diligence is a real possibility. We have estimated, for example, that the Enforcement Office scheme would require a staff of between 300 and 400 full

[1]Section 8.6, p. 49. The Edinburgh University Debtors Survey paras. 9.1 to 9.4 found that of 100 debtors subjected to diligence, 36 sought help from their family and friends who provided financial help in 24 cases. Debtors were reluctant to seek help in cash from people they knew. Very few of these debtors sought cash grants from public agencies (e.g. D.H.S.S.).

[2]In 1983, over 17,000 sheriff court ordinary cause actions for debt were initiated, some of which would have been for sums over £5,000: over 130,000 summary cause actions were initiated of which probably just over three quarters (say 100,000) were debt actions. Information supplied by Scottish Courts Administration prior to publication of the *Civil Judicial Statistics Scotland 1983*.

[3]See para. 2.38 above and Chapter 7 below.

[4]In 1983, over 15,000 summary cause actions for recovery of heritable property were disposed of and an even larger number were initiated: just under 2,000 ordinary cause actions were initiated. Information supplied by Scottish Courts Administration prior to publication of the *Civil Judicial Statistics Scotland 1983*.

time officials to deal with 50,000 cases every year. [1]A debt arbitration service, which would seem to involve twice that number of cases or more, would place an even heavier burden on the public purse.

2.96 *The unco-operative debtor.* In a system where there can be no enforcement without a prior means enquiry, there must be some sanction compelling the debtor to submit to a means enquiry. Otherwise debts would be payable only at the debtor's pleasure. We believe that schemes which depend on compulsory means enquiries seriously under-estimate, first, the extent to which the debtors would fail to co-operate satisfactorily or at all in disclosing their means, and second, the difficulty of the consequential requirement of devising a suitable sanction to compel disclosure. We think it undesirable that a debtor should be compelled to disclose his means, as opposed to making voluntary disclosure a condition of obtaining an order stopping or restricting diligence.

2.97 It is one thing to acknowledge that debtors subjected to diligence are normally willing but unable to pay their debt outright and quite another thing to deduce from that fact that debtors would willingly co-operate in compulsory means enquiries. There would, we think, be a significant number of cases in which the debtor would not comply with the duty of disclosure, especially if it involved attendance at the specialist tribunal or court for oral examination as to his means. One solution suggested was that debt counsellors connected with the specialist tribunal or the court could visit debtors in their homes. This would certainly help to reduce the problem, though it would be expensive to employ a field force to cater for these cases especially since counsellors would often experience difficulty in making personal contact with debtors. Moreover, even when such contact was made, we suspect that an enquiry by an official (whether he be called a debt counsellor or something else) into a debtor's means in his home would often be as much resented as the service of a charge or the execution of a poinding, if not indeed more so.

2.98 There remains the difficult problem of what sanctions should be imposed to compel the debtor to disclose his means. On consultation, those who favoured compulsory means enquiries did not go the length of supporting the imposition of fines or imprisonment as sanctions and we think such sanctions would find little support in Scotland. The number of cases in which such sanctions would have to be imposed might not be great,[2] but it is equally true that the number of warrant sales against household goods is also not great. Some of those who support a debt arbitration service suggested, somewhat inconsistently, that the summary cause procedure should be retained as a sanction against debtors who refused to co-operate. This in itself is not a sanction since a summary cause action does not compel a debtor to do anything. Moreover, this suggestion loses sight of the facts that a summary cause decree is enforceable by diligence and that it is the clear and avowed

[1]See Consultative Memorandum No. 47, Appendix C, para. 28.

[2]It is difficult to know how far the English experience with attachment of earnings orders can be relied on. In England and Wales in 1978 there were about 100,000 applications for attachment of earnings orders: 264 debtors were fined and 160 imprisoned for such offences as failure to attend court. In 1983, there were about 79,000 applications but relatively fewer debtors were fined (130) or imprisoned (55). *Judicial Statistics Annual Report* for 1978 Table F1(b) and for 1983, Table 7.19.

aim of a debt arbitration service, like the other schemes just mentioned, that there should be no enforcement without a prior enquiry into the debtor's means. If there is to be a *duty* of disclosure, as opposed to a *right* voluntarily exercised by the debtor (which is the solution we favour), then there must be some sanction other than diligence in order to give disclosure the character of a duty; we do not believe that a suitable sanction can be devised. Indeed, a system dependent on a compulsory means enquiry would arguably be more, not less, coercive than the present system of court actions and diligence.

2.99 *Prejudicing effectiveness of debt recovery system.* The effectiveness of the present system of diligence, and of debt recovery as a whole, could be adversely affected by a procedure controlling enforcement if that procedure gave real encouragement to those debtors who are able to pay and under the present system do pay their debts, to default in payment or to seek to defer payment. A debt arbitration system of the kind outlined above, for example, although it was not intended that it should benefit debtors who are willing and able to pay, might nevertheless, in practice, encourage such debtors to cease paying their debts promptly. They would no longer be subject to the present economic constraint of liability for the expenses of any court action or diligence occasioned by default in payment and they would have every incentive, especially when interest rates were high, to use the system so as to delay payment. Indeed, there is a real risk that debtors who under the present system pay their debts might be drawn into the debt arbitration scheme to such an extent that the scheme itself might become unworkable. A similar problem might arise under an Enforcement Office system depending on whether it was the policy of the Office to use enforcement against moveable goods as a spur to an instalment settlement, a practice adopted by creditors in Scotland, and (it appears) in England and Wales, but not by the Enforcement of Judgments Office in Northern Ireland.

2.100 *The appropriate forum.* It was a feature of the Enforcement Office and debt arbitration service schemes that they would confer the functions of controlling enforcement on a specialist agency rather than on the ordinary courts of law. In the case of an Enforcement Office, the reasons adduced by the Anderson Report[1] in Northern Ireland and the Payne Report[2] in England and Wales for this policy were not suspicion of the ordinary courts of law but rather administrative and technical considerations. In Northern Ireland, the former bailiffs were generally of low calibre (a criticism which cannot be made of Scottish sheriff officers) and a new public agency was needed. It was desired to have centralised and unified enforcement arrangements whereby all modes of enforcement against all judgment debtors would be controlled by one body. Centralised arrangements would be easier to administer in a small jurisdiction like Northern Ireland (which operates from one set of premises in Belfast) than in Scotland with its larger population and very much

[1]Report of the Joint Working Party on the *Enforcement of Judgments, Orders and Decrees of the Courts in Northern Ireland* (Chairman, A. E. Anderson) Belfast (1965) Parts I to III. The Working Party thought (para. 40) that the Enforcement Office should be responsible to the Head of the Judiciary and to the Parliament of Northern Ireland through the Minister of Home Affairs (now the United Kingdom Parliament and the Lord Chancellor).

[2]Paras. 2.93 *et seq.*

larger area. On consultation, there was little support for the establishment of an Enforcement Office in Scotland.

2.101 The debt arbitration service scheme rejected the courts as the appropriate forum for very different reasons. It seems to have been assumed, first, that the "adjudicatory" role of the courts becomes irrelevant if debts are undisputed; second, that the courts have inherent defects of formality and expense from which specialist tribunals or arbiters are exempt; and third, that courts could not be expected either to devise the particular kind of orders required to regulate or control diligence or to operate procedures which would enable debtors readily to obtain such orders.

2.102 As regards the first of these assumptions, we do not agree that the constitution of a debt by the court is redundant in cases where liability for the debt is not disputed. Some procedure must exist in order to establish whether liability for a debt is admitted or disputed, and since (as is agreed on all sides) the courts must necessarily be the forum for determining liability where a debt is disputed, it seems only sensible that the same forum should be used to establish the prior question whether the debt is indeed disputed or not.

2.103 Second, the assumption that any new powers to control debt enforcement should inevitably be allocated to tribunals rather than the ordinary courts of law (primarily the sheriff courts) is best answered by reference to the observations of the Hughes Report on the respective merits of courts and alternative tribunals.

2.104 Although the Hughes Report recognised that such alternative tribunals (or some of them) might have the characteristics of cheapness, speed and informality, it concluded: "The aim should be to develop in the civil courts themselves those same qualities of cheapness, speed and informality in so far as these are compatible with fair and respected judicial procedures".[1] That conclusion moreover was not reached through any dogmatic attachment to the established court system as such. It was reached rather on the very practical grounds that the court system offered facilities for the purpose which could be augmented, if necessary, at far less cost than would be incurred in providing a wholly new tribunal system. Commenting on small claims procedures, the Hughes Report observed:

> "The advantages of a tribunal are informality in proceedings, the possible appointment of specialist adjudicators, and easier provision for lay representation. On the other hand, we believe that the court system ought to offer similar advantages and that it has other advantages of its own. Only a court can satisfactorily settle matters of substantive law (subject to appeal if this is allowed). The court system offers an existing widespread structure of facilities and personnel that can be augmented, if necessary, at far less cost than would be incurred in providing a wholly new tribunal system."[2]

Significantly for present purposes, the Hughes Report thought that the new court procedure which they recommended for small claims (wherein consumers

[1]Hughes Report, para. 14.6.
[2]*Ibid.*, para. 11.19.

play the role of creditors or pursuers) should supplant the summary cause and thus:

> "also be the 'debt collecting' procedure for the great mass of actions, where there is no dispute about liability, raised, for example, by public utilities and large companies. We believe, however, that most cases of this kind will be settled on paper without an adjudication, as they are now in the summary cause. In any event cheaper procedures mean lower debts, and will be indirectly advantageous to defenders who have to pay expenses. Moreover, we do not want to exclude consumer defenders or small business defenders who at present may concede a strong case for fear of the expense of defending it."[1]

2.105 The practical considerations to which the Hughes Report adverted are particularly relevant in choosing between the courts and alternative tribunals as the appropriate forum for controlling enforcement. It should not be assumed that the debt arbitration service procedures described above would be less formal and therefore less expensive than any court procedure could be. It seems to us that, while arbitration procedures might be less formal than court procedures, they would be likely in practice to be more cumbersome and far more expensive than the very simple procedures which presently apply in undefended ordinary and summary cause actions for debt; and they would impose a new burden on creditors who often would be obliged to attend arbitration proceedings whether the debt was in dispute or not.

2.106 In any event, in relation to both the Enforcement Office and the debt arbitration service schemes, we do not think that, in the present economic situation, it would be realistic to recommend for Scotland a system which would place a heavy additional burden on public funds.

2.107 As regards the third assumption mentioned above, we do not believe that the courts would have any difficulty or hesitancy in making any orders devised for their use in giving time to pay or in relation to the control of enforcement if they had statutory powers to do so. Although the existing law affords only limited opportunities for orders controlling enforcement, the courts have been robust, and indeed innovative, in developing their existing "administrative" powers to grant or refuse warrants authorising the sale of poinded goods.[2] The courts also have wide experience in this domain. It has long been the policy of Parliament, sustained in recent statutes, to confer on the courts powers, exercisable in a wide variety of contexts, of fixing levels of periodical instalments of debts, of giving debtors time to pay, or of delaying or precluding enforcement of debt or repossession of property for that purpose or on social grounds; examples include instalment decrees for debts of small amount;[3] orders for payment by instalments of various consumer debts;[4] orders delaying repossession of goods on hire purchase,[5] or repossession of private or public sector dwellings,[6] to allow arrears to be paid; fixing levels of periodical

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[1] *Ibid.*, para. 11.24.
[2] *S.S.E.B.* v. *Carlyle* 1980 S.L.T. (Sh.Ct.) 98.
[3] Sheriff Courts (Scotland) Act 1971, s. 36(4); cf. Small Debt (Scotland) Act 1837, s. 18.
[4] Consumer Credit Act 1974, s. 129(2)(*a*); Moneylenders Act 1927, s. 18(*f*).
[5] Consumer Credit Act 1974, s. 129(2)(*b*); Hire Purchase (Scotland) Act 1965, s. 35(4).
[6] Rent (Scotland) Act 1984, s. 11(1); Tenants' Rights Etc. (Scotland) Act 1980, s. 15(1).

allowance on divorce and aliment;[1] fixing the amounts and instalments of criminal fines and compensation orders;[2] contribution orders reimbursing public authorities providing various social benefits;[3] fixing contributions by bankrupts out of current income to trustees in sequestration;[4] and discretionary powers to control civil imprisonment for failure to pay aliment or to perform other legal obligations.[5]

2.108 We have, however, been keenly aware that if the courts are to be entrusted with the responsibility for making orders giving debtors time to pay and controlling debt enforcement, the new justice which they will thus administer must, in the words we have quoted above from the Hughes Report, be "accessible justice" and be seen to be accessible in practice by those for whom it is designed. We have therefore carefully considered the measures which would be required to facilitate applications to the court by debtors who seek the protection afforded by the new jurisdiction which we propose. We revert to this aspect of our recommendations below.[6]

2.109 *Main problems of enforcement unsolved.* It should be emphasised that the introduction of a compulsory means enquiry would not solve the problem of what is to happen when a debtor defaults in the payment of sums ordered to be paid by the court or specialist tribunal or arbiter holding the means enquiry. It cannot be assumed that default would not frequently occur merely because the levels of instalments payable by the debtor had been fixed by an independent body following upon a means enquiry. Orders by a specialist tribunal or arbiter, like orders of a court, would still have to be enforced and the legislative choice of methods of enforcement would still be limited, by the lack of any alternative, to enforcement against the debtor's person or his property or income. For this reason, many of the most important problems involved in reforming diligence would not be eliminated but merely put a stage further back in the whole process of debt recovery.[7] In particular, the problems involved in the reform of enforcement against moveable goods would remain. For example, a means enquiry which depends on disclosure by the debtor of his attachable assets is not likely to yield reliable information as to the extent and saleworthiness of his poindable goods. Moreover, the introduction of extremely expensive procedures applying mainly to people who would not suffer poindings anyway, would leave unanswered the questions of whether, in what manner, and subject to what conditions and safeguards, moveable goods should be liable to be attached and sold to satisfy debts.

2.110 For these reasons, we conclude that the disadvantages of schemes making enforcement conditional upon a compulsory enquiry into a debtor's

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[1]E.g. Divorce (Scotland) Act 1976, s. 5; Conjugal Rights (Scotland) Amendment Act 1861, s. 9.

[2]Criminal Procedure (Scotland) Act 1975, ss. 395 and 399; Criminal Justice (Scotland) Act 1980, s. 59(1).

[3]E.g. Social Work (Scotland) Act 1968 ss. 80 and 81; Guardianship Act 1973, s. 11(3); Supplementary Benefits Act 1976, ss. 18 and 19.

[4]Bankruptcy (Scotland) Act 1913, s. 98; *Caldwell* v. *Hamilton* 1919 S.C. (H.L.) 100.

[5]Civil Imprisonment (Scotland) Act 1882, s. 4; Law Reform (Miscellaneous Provisions) (Scotland) Act 1940, s. 1.

[6]Para. 2.134.

[7]This point is made by G. Maher, "The Enforcement of Judgment Debts in Scotland" (1983) 2 Civil Justice Quarterly 244, 256.

means prior to enforcement would considerably outweigh the advantages of such schemes.

(2) Second possible option: debt arbitration on defender "opting out" of court actions and diligence

2.111 A rather different suggestion as to how special procedures for arbitration outside the courts might be used to control enforcement was made on consultation by the Scottish Consumer Council. They did not seek to create a system which would require the intervention of debt counsellors or debt arbiters in virtually every case (as a debt arbitration service would do) nor did they seek to supplant the role of the courts in relation to the constitution of undisputed debt. Instead, they suggested that a procedure should be introduced whereby a debtor would have an option, to be exercised on his own initiative, to refer the question of payment of his debt to a specialist debt arbiter. Debt arbitration in this sense would operate in parallel with the court system and resort could be made to arbitration at any stage in the debt recovery process whether before or after the grant of a court decree. The Council envisaged that a debt arbiter would be a social worker or a solicitor and that he would make his determination on the basis of disclosure by the debtor of the latter's circumstances after a hearing attended both by the debtor and the creditor. In the light of those circumstances, the arbiter would be empowered to make appropriate orders for payment by instalments or otherwise and regulating the execution of diligence.

2.112 We agree with the Scottish Consumer Council that orders restricting or controlling diligence should be dependent on a voluntary disclosure by the debtor of his means rather than on a compulsory disclosure. In two respects, however, we think that this solution does not make the best and most economic use of public manpower and financial resources. First, we think that voluntary applications for orders giving a debtor time to pay and restricting diligence should be confined to cases where a debt action has already been raised or, if a decree for payment has been granted, to cases where the risk of diligence being executed has become real and substantial, as where a charge has been served or diligence otherwise commenced.[1] Second, we think that the same considerations which led us to prefer the ordinary courts of law to debt arbitration in a compulsory means enquiry system[2] apply to debt arbitration in a voluntary scheme and that jurisdiction to make orders restricting or controlling diligence should be conferred on the ordinary courts of law.

(3) Third possible option: summary bankruptcy procedure replacing diligence

2.113 A proposal put to us by the Scottish Association of Citizens Advice Bureaux merits separate consideration: the proposal differed from the other proposals discussed above because (as we understand it) enforcement of debts would have been subsumed within a summary bankruptcy procedure in which a salaried court official would act as a "judicial trustee". It was envisaged that

[1]A charge is always served prior to a poinding and to give debtors an equivalent opportunity to obtain orders restricting diligence before their wages or salary is arrested, we recommend later that a charge should be served prior to an arrestment of earnings: see para. 2.122 and Chapter 6.

[2]See paras. 2.101 to 2.108 above.

where in a debt action the debtor had not entered appearance and was unemployed, "there should be a new step in the debt enforcement procedure after a charge is served whereby there is an obligation on the creditor to explain to the sheriff the debtor's situation". A new office, whose incumbent would be a salaried official called a "judicial trustee", would be created. The judicial trustee would "evaluate the debtor's resources and outgoings" and would also enforce debts in place of sheriff officers. It was envisaged that "enforcement should be subject to the control of the court but with a wider discretion than at present and should be carried out under a summary bankruptcy procedure". The creditor "should be required to approach the sheriff with information about the debtor's situation after the charge had been served but before the poinding". The sheriff would have power to authorise and restrict diligence.

2.114 The proposal understandably was put to us in very general terms and it may be that we have not understood it fully but, giving the proposal as fair consideration as we can, we have concluded that it would not be satisfactory or practicable. First, in the great majority of cases, the creditor would not be in a position to explain the debtor's situation. He would often not know if the debtor was employed and would almost certainly have no detailed knowledge of the debtor's resources or commitments. In almost all cases, only the debtor can explain his financial position to the sheriff. A compulsory means enquiry would therefore be essential, entailing all the disadvantages which we identified above. Second, as we explain in Chapter 4 when discussing debt arrangement schemes, bankruptcy procedures, involving among other things the vesting of assets in a trustee, are cumbersome, expensive and quite inappropriate for consumer debtors, most of whom do not have sufficient assets to make the procedure worthwhile.[1] They would often be particularly inappropriate where only one debt was being seriously pursued to the stage of decree and diligence which is in fact the usual case. Third, if, as seems likely, most consumer debtors would dislike the stigma of bankruptcy as much as the stigma of poinding and warrant sale, it is very doubtful whether the proposal would achieve its social policy aims. Fourth, in any event under the Bankruptcy (Scotland) Bill presently before Parliament, an insolvent debtor will be entitled to apply for his own sequestration with the concurrence of one qualified creditor.[2]

Section E. Our preferred option: discretionary control of diligence by ordinary courts of law on voluntary application by debtor

2.115 Although we have criticised various aspects of the schemes described above for the discretionary control of diligence, we agree with the proponents of these schemes that the primary aim of reform should be to make the operation of the system of debt enforcement more humane in its impact on debtors and their families while preserving the effectiveness of the system as

[1]The proposal seems to have contemplated "bankruptcy" in the sense of sequestration of assets because the proposal differentiated its bankruptcy procedures from our own proposals for debt arrangement schemes which would not involve vesting of assets in the administrator of the scheme.

[2]Bankruptcy (Scotland) Bill 1984, clause 5(2)(*a*) (see para. 1.15 above). Under the present law, an insolvent debtor can apply for his own summary sequestration.

a means of debt recovery: the debate concerns the means of achieving that aim rather than the aim itself.

2.116 If we are right in not accepting the foregoing schemes, then the correct path to reform must lie in evolving a system which would allow the creditor to pursue his debt by court action and diligence as under the present law but would permit the debtor to apply to the court for one or more orders controlling diligence. The courts would continue to have jurisdiction in entertaining debt actions and in authorising diligence when granting decree for payment. The courts, however, would also be given an important new jurisdiction to control diligence at appropriate stages of the debt recovery process. That process, with its filter effect, would remain, but subject to this new jurisdiction and to the reforms of the modes of diligence mentioned later. A debtor's disclosure of his means to the court would not be a compulsory prelude to enforcement by diligence but rather a condition of a voluntary application by the debtor to the court for the control of diligence.

2.117 We believe that it is possible to frame, on these lines, a system of discretionary control of diligence:

(*a*) which would make the best and most economic use of resources (for which the public or parties must pay) by using the existing court structure and by restricting court procedures to cases either where debt actions were pending or where the risk of diligence had become real and substantial;

(*b*) which would avoid any need to impose sanctions (such as the inappropriate penalties of fines or imprisonment) on unco-operative debtors other than liability for the expenses of diligence and would therefore be less coercive in important respects than a system of control based on compulsory means enquiries; and

(*c*) which would by and large preserve the effectiveness of the present system of debt recovery and diligence from the standpoint of creditors, (dependent as it is on the sanctions underlying the gradual evolution of a protracted debt recovery process giving debtors who can do so ample opportunity to pay), while giving debtors unable to pay a debt outright much greater opportunities and rights than under the present system to obtain an extension of time to pay and safeguards in appropriate cases from existing or threatened diligence procedures.

A number of important issues, however, remain including questions as to what types of order controlling diligence should be available; the precise stages in the debt recovery process at which debtors' applications for control of diligence should be permitted; and what procedural and other reforms are needed to make the orders controlling diligence readily available to those debtors for whose protection they are designed.

2.118 We consider these questions next. Although we believe that our proposals on discretionary orders and the reform of diligence would make a better use of resources than the proposals rejected in Section D, nevertheless we do not suggest that it would be possible to accommodate all our recommended reforms within the resources currently available to the courts. We would emphasise that some increase in resources would be required and

unless these extra resources were made available, some at least of our proposed reforms would in practice be unworkable.

New orders controlling diligence and giving time to pay

2.119 In the reformed system of debt enforcement which we recommend, debtors would look to the ordinary courts of law, generally the sheriff court, for protection from the rigours of diligence. This requires that important new powers should be conferred on the courts enabling them to give debtors the required degree of protection. At the heart of the reformed system, therefore, would be a range of new orders which the court in its discretion would be empowered to make in appropriate cases on the application of the debtor. We envisage that these orders would consist of the following:

(*a*) *Time to pay decrees,* which would provide for payment by instalments or a deferred lump sum and stop diligence during the period allowed for payment. Such decrees would be available in debt actions against individuals in the Court of Session and sheriff court where the sum payable under the decree does not exceed £10,000. These decrees would replace summary cause instalment decrees.[1]

(*b*) *Time to pay orders* which would convert "open" decrees (i.e. decrees for payment in a lump sum) into decrees having similar effects to time to pay decrees, would be introduced for the first time in Scots law. Whereas time to pay decrees would be available in court actions, time to pay orders would be available at the later stage when a charge to pay had been served on the open decree. They would also be available where a summary warrant for rates or taxes had been granted, or diligence (e.g. arrestment) had been used.

(*c*) *An order confirming a debt arrangement scheme* which would be a new insolvency process providing for (i) the orderly and regular payment by a multiple debtor of the debts due to his several creditors, (ii) the discharge of debts in appropriate cases on payment of a composition of less than 100p in the pound, and (iii) the prevention of diligence and bankruptcy proceedings against the debtor by creditors included in the scheme and all other creditors for civil debts while the scheme was in operation.

(*d*) *Orders in diligence processes:* the courts would be given powers to make new types of orders in poindings, earnings arrestments and summary warrant diligence including *orders recalling poindings* made, on the debtor's application, on certain equitable grounds.

In the following paragraphs, we briefly describe the main features of these new safeguards for debtors and thereafter we deal with the very important question of how such safeguards may be made readily accessible to debtors.

(a) *Time to pay decrees and time to pay orders (Chapter 3; draft Bill, Part I)*

2.120 The principles underlying time to pay decrees and time to pay orders, in particular the introduction of time to pay orders after charges are served or diligence executed in pursuance of decrees, were discussed in our

[1]See paras. 2.26 to 2.27 and 2.61 for the existing provisions on summary cause instalment decrees.

Consultative Memorandum No. 48 and all who commented on the topic agreed that such decrees and orders should be introduced in Scots law. We discuss the arguments and describe our proposals in more detail in Chapter 3.

2.121 We have emphasised that to hold a *compulsory* means enquiry in every case where at present an action for payment is raised or diligence instructed would be unrealistic since it would overload the courts with the function of investigating the means of too many debtors who are able to pay or whose cases would not in any event proceed to diligence. By contrast, a system of *voluntary* applications to the court for time to pay decrees and time to pay orders would, we envisage, normally involve a simple "paper procedure" whereby an offer to pay by instalments would be transmitted to the creditor and in making such an offer, the debtor could, but need not, disclose his means. Only if agreement was not reached as to whether a time to pay decree or order should be made, or as to its terms, would the court, if so advised, require a hearing in which the debtor would have to satisfy the court as to his inability to pay immediately in a lump sum. The courts would not be overloaded by unnecessary means enquiries and the need to invoke inappropriate sanctions, such as fines and imprisonment, would simply not arise.

2.122 We think it appropriate that time to pay decrees should be competent in court actions because the case is already before the court and it is reasonable that the court should be able to deal with the question of the debtor's ability to pay at that stage. Where court actions relating to the debt are not actually proceeding, we think that applications for time to pay and control of enforcement should not be possible until a stage is reached in the debt recovery process at which the risk of the creditor instructing diligence has become real and substantial: otherwise there would be a waste of resources. Accordingly, we propose that while time to pay decrees should be available in the court action, a time to pay order should be available at the later stage when the creditor has proceeded to the next formal step in debt recovery following the grant of decree. In the case of poinding and warrant sale procedures, this stage is the service of a charge by the officer of court which gives the debtor a period (which we think should be standardised at 14 days[1]) in which to settle the debt and warns him of the possibility of poinding in the event of non-payment. There is at present no comparable procedural stage in the case of arrestments of earnings (or indeed other arrestments). We have therefore recommended in Chapter 6 that the service of a charge should be a precondition of an earnings arrestment so that there will be an appropriate stage at which an employed debtor whose earnings are threatened by arrestment can apply for a time to pay order precluding such an earnings arrestment and, indeed, any other diligence for so long as he complies with the order. The service of a charge would also be an opportune time at which to notify the debtor of the availability of the new safeguards against diligence. In other cases an application would be competent where a diligence (e.g. an arrestment of funds other than earnings) was executed or begun, or where a summary warrant for recovery of rates or tax arrears was granted.

2.123 The privilege of extension of time to pay debts conferred by a time

[1]See Recommendation 5.2 (para. 5.12); Bill, clause 115(2).

to pay decree or time to pay order would be matched by restrictions on creditors' rights to commence new diligences or continue with existing diligences for so long as the time to pay provisions had not lapsed through the debtor's default[1] or been recalled on a change of circumstances. Thus it would generally not be lawful for the creditor to execute new diligences to enforce the debt. This restriction would apply to poindings, earnings arrestments and other arrestments and to adjudications of heritable property but not to inhibitions. Secured creditors' diligences and remedies (such as poinding of the ground or sequestration for rent or feuduty) would not be precluded. Practical considerations require that a time to pay order should not be competent when a particular diligence had reached an advanced stage (e.g. a poinding had been followed by a warrant of sale or an arrestment by decree of furthcoming) until that diligence was completed. Apart from that, time to pay decrees and orders would affect diligences already begun: the court would have a range of duties and powers to recall or restrict existing diligences and any existing diligence not recalled would be "frozen". Thus, when a time to pay order came into force, existing earnings arrestments would be recalled, and a poinding or arrestment of money, if not recalled by the court, could not be followed by warrant of sale or action of furthcoming (as the case may be) while the time to pay order was in force.

(b) *Debt arrangement schemes (Chapter 4; draft Bill, Part II)*

2.124 There is one problem in the field of debt recovery which we think could, and should, be mitigated by the introduction of a new legal procedure. This is the problem of multiple indebtedness. We have already noted that the normal pressures of diligence on a debtor may be aggravated where his several creditors enforce their debts by court actions and diligence simultaneously.[2] We have in view mainly consumer debtors and small traders. Such debtors rarely have sufficient assets to make sequestration under bankruptcy legislation worthwhile and in any event sequestration is a drastic remedy for an over-committed consumer debtor. Multiple indebtedness can also present problems for creditors despite the existing rules on equalisation of diligences outside sequestration[3] which are rarely invoked at any rate in cases of diligence against earnings or poindings of household goods. This may work to the disadvantage of the considerate creditor who gives the debtor time to pay. The main problem, however, is that there is no procedure which a multiple debtor can initiate for compelling his creditors to accept arrangements for the orderly and regular payment of his debts.

2.125 Although the research conducted for this report suggests that multiple debt problems may be less common than might be supposed (inasmuch as there appear to be relatively few cases in which two or more debts of a multiple debtor reach the diligence stage simultaneously),[4] we think the

[1]The provisions on automatic lapse by default are modelled on summary cause instalment decrees with modifications in the debtor's favour. Moreover, any default in payment of an instalment would not lead to the lapse of the right to pay by instalments unless the decree had been intimated to the debtor before the default occurred: see Chapter 3 at paras. 3.43 to 3.46.

[2]Para. 2.71 above.

[3]Bankruptcy (Scotland) Act 1913, s. 10 to be replaced by the Bankruptcy (Scotland) Bill 1984, Sched. 7, para. 10.

[4]See paras. 4.2 to 4.5 below.

problems are sufficiently acute to call for legislative intervention. In Chapter 4, therefore, we recommend the introduction in Scots law of a new insolvency process designed particularly for wage and salary earners and small traders in multiple debt, to be called a debt arrangement scheme. While provisional proposals to introduce such schemes in our Consultative Memorandum No. 50 evoked a mixed response on consultation, we think that there is a gap in Scots law which debt arrangement schemes would fill, and we are fortified in this view by a comparison with other countries where similar procedures have been introduced by legislation or recommended by official advisory bodies.[1]

2.126 We envisage that a debt arrangement scheme would have the following main features:

(*a*) The overall object of the scheme would be to allow a debtor an extension of time to pay his debts in reasonable instalments over a maximum prescribed period, normally three years with possible extension to five years in all, during which the debtor's compliance with the scheme would be supervised by an administrator appointed by the sheriff.

(*b*) All creditors in existing and future debts would be generally precluded from doing diligence or petitioning for sequestration while the scheme operated. Existing diligences would be recalled unless they had reached an advanced stage in which case the sums disbursed to the creditor would be reduced by an amount equal to the net proceeds of the diligence.

(*c*) The scheme containing the debtor's proposals for payment of all his civil debts would be submitted in draft to the creditors and would only come into operation on being confirmed by the sheriff after hearing any objections by creditors.

(*d*) During the currency of the scheme, the administrator (who would normally be the sheriff clerk or a member of his staff) would collect payments due by the debtor under the scheme and disburse them to the creditors who would all rank *pari passu* (rateably) on disbursements, with special provision being made for contingent and other creditors included later during the life of the scheme.

(*e*) The sheriff would have power to order deductions of appropriate amounts from the debtor's earnings to be made by the employer and paid to the administrator for disbursement to the creditors.

(*f*) The scheme would provide either for payment in full of the debts or in appropriate cases for a composition of less than 100p in the pound. The debtor would only obtain a discharge of debts at the end of the scheme if he had complied with it.

The main differences from sequestrations would be that the very complicated rules for ranking preferred and secured creditors in bankruptcy would not apply and that the debtor would not be divested of his assets, though he might be required by the scheme to sell specified assets, the proceeds of which would be distributed to the creditors by the administrator.

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[1]See para. 4.31 below.

2.127 Clearly such a process would require a full means enquiry and, in consonance with our view that compulsory means enquiries should not be required outside sequestration, a scheme should not be made except on the voluntary application of the debtor who would have to make a full disclosure of his means as a condition of obtaining a scheme. Debt arrangement schemes are clearly more suitable for wage or salary earners than for poor unemployed debtors. Difficult questions therefore arise as to whether multiple debtors who can afford to pay only very small amounts (e.g. unemployed debtors) should be entitled to apply or whether the availability of schemes should be restricted, at least until experience of the working of the schemes in practice has been obtained, to cases where the likely yield to creditors would justify the public expense and the work involved on the part of the court and the administrator. We think however that it would be unrealistic to recommend schemes which yield nothing or almost nothing for the creditors.

(c) *Other orders controlling diligence*

2.128 As we indicated above,[1] time to pay decrees, time to pay orders and debt arrangement schemes would be of wide and general application in their effect on diligences enforcing the debt or debts concerned, and indeed would affect diligences of all types with minor exceptions.[2] In addition to these general safeguards for debtors, specific reforms of the main modes of diligence—poinding and sale and arrestment of earnings—would be made, including the conferment of powers on the sheriff to make orders recalling, or releasing goods from, a poinding. One such power is of particular importance in the present context. This is the new power which we propose for the sheriffs to make an order (on the debtor's application) recalling a poinding on the same grounds as, under our recommendations, he could refuse to grant warrant of sale at the later stage when the creditor applies for such a warrant (broadly, undue harshness, low valuations or the likelihood that the proceeds of a warrant sale would not cover the expenses of applying for and executing the warrant).

Orders declaring debts unenforceable on ground of debtor's inability to pay?

2.129 In our Consultative Memorandum No. 48,[3] we sought views on whether the courts should be given a power to make an order declaring a particular debt to be unenforceable in whole or in part on the ground of the debtor's inability to pay. The order, we thought, should be capable of variation or recall on a change of circumstances. Such a declarator, we envisaged, would in most cases be an order rendering part of the debt unenforceable and would normally be combined with an order allowing the balance of the debt to be paid by instalments. Such an order has a parallel in the Northern Ireland certificates of unenforceability[4] and in the enforcement restriction orders

[1]See paras. 2.123 and 2.126(*b*).

[2]E.g. heritable creditors' diligences and diligences which had proceeded to an advanced stage, e.g. warrant of sale or decree of furthcoming, would not be affected, while the new diligence of current maintenance arrestment would be affected by debt arrangement schemes but not by time to pay decrees or orders.

[3]Para. 1.22 and Proposition 1 (para. 1.26).

[4]Judgments Enforcement (Northern Ireland) Order 1981, articles 18 and 19 (S.I. 1981/226).

recommended by the Cork Report for England and Wales.[1] This proposal evoked a mixed response on consultation and on reflection we think that it should be rejected. A combined unenforceability and instalment order would, in practical effect if not in theory, operate to allow a kind of discharge on payment only of a composition and, as the Law Society of Scotland observed to us, such a compulsory composition should not in principle be imposed on creditors outside insolvency proceedings. Compositions in debt arrangement schemes would apply to all creditors, whereas a composition of this kind would only apply to the creditor whose debt was affected by the unenforceability order. We think that this would be discriminatory and unjust to that creditor. Moreover, the appointment of an administrator can be justified in debt arrangement schemes (which would affect all debts), but could not be justified in unenforceability orders (since they would affect only one debt), which therefore could not be properly supervised.

2.130 We are aware that unless debt arrangement schemes are made available to debtors who can afford to pay only very small sums towards the satisfaction of their debts, the anomaly may arise that discharges on payment of a composition would be available to debtors who, though insolvent, have at least some income or assets, whereas such discharges would not be available to the poorest debtors, with no assets, dependent on social security. The poorest debtors, however, are at risk mainly from poindings of household goods and if they are conceded the right to apply for recall of a poinding, they will attain in substance the same protection as would have been afforded by a declarator of unenforceability having regard to the restrictions on second poindings in the same premises for the same debt.

2.131 Furthermore, while we think that an order extending time to pay may be appropriate even though the creditor has not ascertained the extent of the debtor's poindable assets, we do not see how a sheriff could feel justified in declaring a debt to be unenforceable if he had not had the opportunity of verifying the debtor's moveable goods by examining a report of a poinding (containing valuations by the officer of court which the debtor could challenge if so advised). In our view, therefore, a right conferred on a debtor to apply for recall of a poinding, exercisable after the poinding was executed, would have this great advantage over an application for a declarator of unenforceability that the inventory and valuations in the report of poinding would always be available to the court in applications of the former type but not in the latter. For these reasons, we recommend that declarators of unenforceability should not be introduced.

Orders declaring debts unenforceable on ground of creditor's fault in extending credit?

2.132 In our Consultative Memorandum No. 47, we referred to an argument that consumer debt should not be enforceable by diligence if the creditor can be said to have been at fault in extending credit to the debtor in the first place. We noted that representations had been made to the Payne Committee that "some curb should be placed upon creditors who enter into rash, speculative

[1]Paras. 309 and 310.

or irresponsible transactions with judgment debtors".[1] We sought views on whether the court should be empowered to make an order rendering a consumer debt unenforceable by diligence if, at the time of extending credit, the creditor had omitted to make enquiries as to whether the debtor was an undischarged bankrupt, or had a recent decree for payment pronounced against him, in order to establish the debtor's creditworthiness. This proposal received little support on consultation.

2.133 We have come to the conclusion, which is supported by the Payne and Crowther Reports,[2] that legislation on these lines would not be justifiable. It would in effect impose a burden upon creditors not only to make enquiries as to the creditworthiness of a debtor before extending credit, but also to keep a record of those enquiries. Thus, to take a simple example, a plumber who mended a tap for a customer on credit might be at risk unless he made appropriate enquiries as to the customer's credit standing and then kept a record of these enquiries. We think that the disruption which the consequent burden on creditors would cause to the credit system as a whole would be unacceptable. The enquiries might often be resented by the recipients of credit, the majority of whom are creditworthy and pay their debts. Moreover, such enquiries would have no relevance in those many cases where the debtor's default was attributable either to events arising after the original extension of credit or to circumstances which no enquiry into creditworthiness could have revealed. We do not therefore make any recommendation that diligence should be made conditional upon the prior making of enquiries into the creditworthiness of the debtor at the time when credit was extended.

(d) *Assisting debtors to obtain the protection of the court*

2.134 We have already observed that the new justice to be administered by the courts must be accessible justice and appear as such to those for whom it is designed. The formulation of procedural rules and other measures which would put the new safeguards within reach of debtors presents difficulties which must be solved if reform is to be successful. It was, of course, awareness of precisely these difficulties which inspired the proposals by some consultees to establish specialist tribunals or arbiters, but other consultees who envisaged that control of enforcement should remain with the courts also emphasised the need for such measures.[3]

2.135 The research into debtors' circumstances discloses that debtors often find it difficult to understand the terminology of legal documents, the nature of the procedure of court action and diligence and its possible impact on

[1]Payne Report, para. 849; also para. 56. The Crowther Report para. 6.4.1. remarked that "all too frequently, credit is extended to those who on subsequent inquiry have been found not to be worthy of credit and indeed who have previously defaulted on numerous credit transactions".

[2]Payne Report, para. 853; also Crowther Report which recognised (at para. 3.6.15) that credit grantors should be *encouraged* to make proper enquiries but did not propose that creditors should be penalised for failing to make such enquiries, and observed "that consumer insolvency in Britain has not at present become such a serious problem that we need to consider the desirability of controlling the availability of consumer credit to all in order to protect the minority of defaulters".

[3]For example, the General Council of the Scottish Trades Union Congress remarked that "the existing Court system and procedures do not encourage people to use the Courts to settle debt problems".

them.[1] Further, more debtors would benefit from instalment decrees than the small number (16% or thereby) of defenders who in fact apply for summary cause instalment decrees.[2] On the other hand in more recent times party litigant procedures have been and are successfully operated by the Scottish courts e.g. in the field of divorce[3] and the recent small claims experiment in Dundee.[4] Moreover, experience in certain court districts of the security of tenure provisions in the Tenants' Rights Etc. (Scotland) Act 1980, Part II, shows that rent defaulters under threat of ejection will come to court in large numbers in order to obtain a breathing space in which to pay off their rent arrears, if publicity is given to their rights to apply to the court and if they are encouraged to approach the court by social work departments, other helping agencies, and district councillors.[5] Furthermore, under our recommendations the debtor's application for control of diligence will be permitted not only, as under the present law, at the court action stage (when the prospect of diligence may seem remote) but also when diligence is imminent and even after it has begun. All these factors suggest that the reluctance of debtors to approach the courts for protection can to a great extent be overcome.

2.136 We envisage that the forms and procedures would be kept simple and that the procedure should be capable of being initiated and pursued with the help of the court by ordinary persons unfamiliar with court procedures, including persons of lower than average capacity in managing their affairs. Though legal advice and assistance should continue to be available, we think that debtors facing actions for debt and diligence would as at present generally not turn to solicitors for help.[6] We do not think that, as a general rule, legal aid should be available to ensure representation of debtors by solicitors; legal aid applications would unduly delay the execution of diligence and the issues involved in giving time to pay and controlling diligence can, we think, be generally resolved without involving the professional skills of solicitors at the expense of the public purse. Legal aid should therefore be restricted to a limited class of exceptional cases such as appeals on points of law and proceedings concernings breaches of poinding or the rights of third parties in poinded goods.

2.137 To assist unrepresented debtors in obtaining the protection of the court, our recommendations include a variety of measures:[7]

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[1]E.g. Edinburgh University Debtors Survey, paras. 5.1 to 5.9; O.P.C.S. Defenders Survey, para. 8.8.

[2]See para. 2.27.

[3]See Doig and Jones, *The Simplified Divorce Procedure* (1984) Scottish Office Central Research Unit Papers.

[4]See Connor and Doig, *A Research Based Evaluation of the Dundee Small Claims Experiment* (1983) Scottish Office Central Research Unit Papers.

[5]See Adler, Himsworth and Kerr, *Public Housing, Rent Arrears and the Sheriff Court* (1985) Scottish Office Central Research Unit Papers.

[6]The O.P.C.S. Defenders Survey (p.53) found that almost two thirds (63%) of defenders in debt or debt-related actions did not seek help or advice from any source. The remaining 37% sought advice from the following sources: friends or relatives (13%); solicitor or lawyer (9%); Social Work Department (9%); social security office (7%); Citizens Advice Bureau (3%); creditor (1%); other sources (3%).

[7]See paras. 9.27 to 9.31.

(1) The new powers of control of enforcement would as a general rule be exercised by the sheriff even where the decree being enforced had been granted by the Court of Session.[1]

(2) Debtors must not be deterred from lodging applications for time to pay and control of diligence by fear of incurring expenses of unforeseeable amounts. Accordingly, as the Law Society of Scotland suggested, court dues should not be exigible,[2] and in proceedings between the debtor and creditor not involving third parties, debtors should generally not be liable for the expenses of creditors (or vice versa) with the necessary exception that frivolous applications could, at the court's discretion, be penalised by an award of expenses not exceeding a prescribed sum.[3]

(3) It can be confidently predicted that court staff would give information to debtors who sought it as to the procedures for making applications, and in addition sheriff clerks should be under an express statutory duty to assist debtors in completing forms of application.[4]

(4) Once an application by a debtor for a time to pay order, or recall of a poinding, or other safeguard had been lodged, the service of forms on the creditor and any other parties would be effected by the sheriff clerk.[5] In debt arrangement schemes, the preparation of a draft scheme embodying the debtor's proposals for payment and the various procedural steps would be undertaken by the administrator.[6]

(5) Rules of court should be made allowing lay representation of debtors at any hearings before the sheriff.[7]

(6) Forms served on or used by debtors should be prescribed by rules of court and should be in simple and intelligible language.[8]

(7) At appropriate stages in diligence procedures, forms served on or delivered to debtors (such as charges or poinding schedules) should notify the debtor of his rights to apply for the new discretionary orders controlling diligence.[9]

2.138 We carefully considered an imaginative proposal put to us by the Law Society of Scotland for a new integrated procedure whereby the various orders safeguarding debtors would be made available in a single process initiated by the debtor lodging a simple form of application listing all his debts and seeking the exercise of the court's jurisdiction without specifying the type of order (e.g. time to pay, debt arrangement scheme, recall of poinding, etc.) which he wished the court to make. In other words, the debtor would simply emit a sort of "cry for help" leaving it to the sheriff to decide what type of order

[1]See e.g. Bill, clauses 4 and 9 (time to pay orders); 14 (debt arrangement schemes); 49 (recall of poinding); 52 (warrant of sale); 78 (recall of earnings arrestment); 83 (recall of current maintenance arrestment); 92 (recall of conjoined arrestment orders).

[2]Recommendation 9.6(5) (para. 9.31), Bill, clause 121(1).

[3]Recommendation 9.8(1), Bill, clause 117 and Sched. 1, paras. 7–9; Sched. 6, paras. 28–30. Debtors would however be liable for the expenses of one application by a creditor for warrant of sale: Bill, Sched. 1, para. 1(1)(*g*).

[4]Recommendation 9.6(1) (para. 9.31); Bill, clauses 5(2) and 121(2).

[5]E.g. Bill, clauses 5(5), 6(4), 49(4) and (5).

[6]Bill, clauses 19–32.

[7]Recommendation 9.6(2) (para. 9.31); Bill, clause 122.

[8]Recommendation 9.6(4) (para. 9.31).

[9]Recommendation 9.6(3) (para. 9.31).

was appropriate in the circumstances. We were initially attracted by this proposal since it seemed to provide a solution to the problem of making the protection of the court readily available to debtors.

2.139 Having examined the practical implications of this proposal, however, we think it is open to serious objections. First, we think that the burden on court resources entailed by the integrated procedure would make it quite impractical. Since the information as to means and debts which forms of application would embody would be unverified and too brief to serve, by itself, as the basis of a decision choosing the appropriate form of order, it appears to have been envisaged—and would certainly seem an essential step in the procedure—that every case would involve an interview or hearing before the sheriff or an enquiry into the debtor's means. It appears therefore that every case, even single debt cases, no matter how simple, would have to pass through a procedure which would have many of the complications of an application by a multiple debtor for a debt arrangement scheme, even if the sheriff decided ultimately to treat the case as appropriate only for a time to pay order, or other order affecting a single debt. Second, it seems to us that this cumbersome procedure would be quite unnecessary in many cases where only one debt had reached the stage of court action and diligence and in all cases where the debtor knew what type of order he wanted. The number of such cases should not be under-estimated. We think that the solution under-estimates the ability of debtors to choose the order they seek from what will be a limited field of choice. Third, under our proposals, forms of application could be prescribed which set out the type of order sought, and there would be nothing to stop a debtor from applying for two or more such orders simultaneously. We have therefore come regretfully but nonetheless firmly to the conclusion that an integrated procedure on the lines suggested should not be adopted.

Section F. Reform of poindings and warrant sales, diligence against earnings, and summary warrant diligence

2.140 The new discretionary orders just discussed—time to pay decrees, time to pay orders and debt arrangement schemes—would provide very important safeguards for debtors unable to pay their debts outright. These orders would affect in principle all diligences enforcing unsecured debts. There remains, however, the problem of what is to happen in circumstances (which may frequently occur) where unfortunately a debtor defaults in payment under one of these orders or where a debtor in financial difficulties fails to obtain such an order, and enforcement by diligence becomes necessary. Since the impact of diligence on debtors—especially the later stages of poinding and warrant sale procedures—lies at the root of the public concern about diligence, the solution of this problem is clearly of central importance. Arrestments of earnings also require reform partly because of their severe financial impact on debtors and partly because their limitation to one pay packet makes them relatively inefficient from the standpoint of creditors. These problems are left unsolved by the introduction of discretionary orders stopping diligence pending payment arrangements. We consider therefore that reforms require to be made to these two modes of diligence and also the special forms of poinding authorised by summary warrants for the recovery of rates and taxes.

2.141 Before outlining our approach to the reform of these diligences, a preliminary question arises concerning the scope of this report and the relationship between diligence and social security payments. At present, the wide range of social security benefits, pensions and allowances payable by the Department of Health and Social Security and unemployment benefit payable by the Department of Employment are exempted from diligence by statute[1] and probably also by the common law.[2] Partly as a result of these exemptions, the poinding of goods in the debtor's residence is sometimes used as a means of bringing pressure on a debtor to pay his debts out of social security receipts.[3] As a consequence, it has been suggested that the present system whereby diligence is used in this indirect way to elicit payment from social security receipts might be replaced by arrangements which would enable small amounts from social security to be attachable for debt on analogy with the arrangements whereby deductions from the weekly rate of supplementary benefit may be paid direct to a fuel authority or a local authority landlord. As we indicated in our Consultative Memorandum No. 47,[4] however, this proposal goes beyond the reform of diligence and relates mainly to the amendment of social security law[5] which could only be appropriately considered by an advisory body if it had United Kingdom terms of reference. We therefore proceed on the assumption that social security and other statutory benefits will continue to be exempt from diligence. We would add however that our recommended reforms should change the position: the widening of the exemptions from poinding to cover all necessary household goods should make it less necessary for debtors to seek social security exceptional needs payments to preserve such goods from poinding, and it would be for consideration whether the new orders giving an insolvent debtor time to pay and precluding diligence would in any event be preferable to the arrestment or diversion of his social security income to private sector creditors, albeit that payments under such orders would presumably come from social security income.

(a) Reform of poindings and warrant sales (Chapter 5: Bill, Part III)

(i) *Reform or abolition?*

2.142 Our consultation revealed widespread dissatisfaction with aspects of the present law and practice of poindings and warrant sales. We were strongly urged by some of our consultees that, on social grounds, abolition was required rather than reform. We would emphasise at the outset that we have no doubt that the diligence as it presently operates does indeed require very substantial reform; and we hope that our recommendations for modernisation and reform of the diligence will allay the concern of many who have argued for its abolition.

2.143 Some of the demands for abolition seem to have been based, at least

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[1]See e.g. Child Benefit Act 1975, s. 12; Social Security Pensions Act 1975, s. 48; Supplementary Benefits Act 1976, s. 16.

[2]*Sinton* v. *Sinton* 1976 S.L.T. (Sh. Ct.) 95.

[3]As might be expected, poindings against recipients of supplementary benefit and other forms of social security are common, but see para. 2.153, footnote.

[4]Paras. 3.7 to 3.10.

[5]For example, if new diversion arrangements for social security benefits were to be seriously considered, one option would be to make the benefits assignable by the claimant rather than arrestable by the claimant's creditor.

in part, on certain misunderstandings. For example, it is a mistake to assume that the diligence of poinding is an anachronistic survival from a harsher era simply because a vernacular Scots term of venerable age is used to denote that method of enforcement.[1] Moreover, there is no foundation at all for the belief that enforcement against moveable goods in the debtor's possession is somehow peculiar to Scotland: on the contrary, enforcement against moveable goods is permitted in every country of whose practice we are aware. Indeed, in England and Wales, execution against goods, including household goods in debtors' dwellings, is by far the most commonly used method of enforcing judgment debts,[2] and if one compares the numbers of county court warrants for execution with the sales executed, it appears that the English procedure has a filter effect not unlike that in Scotland.[3] Moreover, so far as the procedures allow comparisons to be made, the extent to which creditors rely on enforcement against goods as compared with enforcement against earnings is much greater in England and Wales than in Scotland.[4] Any cross-border differences in public attitudes to enforcement against goods, therefore, are probably explicable by reference to procedural differences: for example, in England sales are generally held in auction rooms, not as in Scotland in debtors' dwellings. Given that the Scottish procedures were last revised in 1838,[5] it would be surprising if some reforms were not now necessary. However, pejorative epithets sometimes used in public debate (such as "barbaric", "mediaeval" or "Dickensian") seem to us out of place when applied to the concept of enforcement against moveable goods as such, however much they may be justified in relation to specific aspects of the diligence procedure, such as sales in the debtor's home and the prior advertisement of such a sale.

2.144 Moreover, in considering whether a particular mode of enforcement has outlived its usefulness and is ripe for abolition, there is an important limiting factor which must be borne in mind. Every society which holds to the belief that people able to pay their debts should be required by law to do so must make available to creditors modes of enforcement from a field of choice which is limited by economic and social realities to diligence against the debtor's person (i.e. civil imprisonment for debt), or diligence against his heritable or moveable property or his income. All these modes of enforcement

[1] "Poinding" is simply the old Scots word for "impounding" (Scottish National Dictionary, vol. vii, s.v. "poind") though nowadays poinded goods are not impounded but left in the debtor's possession.

[2] In England and Wales, in 1983, over one million (1,148,001) county court warrants for execution against goods to enforce judgment debts were issued as compared with under 80,000 applications for attachment of earnings orders enforcing judgments (79,280) and under 43,000 attachment of earnings orders made (42,612): *Judicial Statistics Annual Report 1983* (Cmnd. 9370) Tables 7.18 and 7.19.

[3] In 1983, there were 1,148,001 county court warrants of execution against goods and as few as 3,633 sales made. In 1982, the corresponding figures were 1,059,590 warrants and 2,919 sales made: *ibid* Table 7.18.

[4] For example, in 1978 (the only year for which statistics on arrestments of earnings are available and comparisons can be made) for every attachment of earnings order there were about 20 warrants of execution against goods in England and Wales. By contrast, in Scotland for every "first" arrestment of earnings there were as few as seven or eight charges (the first step in diligence against goods).

[5] See the Debtors (Scotland) Act 1838, some of whose provisions had been enacted earlier in the Bankruptcy Act 1793 (c. 74) (otherwise known as the Payment of Creditors Act 1793), s. 5; and the Bankruptcy Act 1814 (c. 137) s. 4.

are necessarily coercive and in any given legal system at any given time it frequently happens that a particular mode of enforcement is especially unpopular. For example, in England in the 1960s, civil imprisonment for debt was much criticised and it was abolished in 1970 as a mode of enforcing ordinary judgment debts.[1] It was found, however, that abolition by itself would have left a gap in the enforcement procedures available to creditors under English law. Accordingly, attachment of earnings (which had been abolished in England a century earlier[2]) was re-introduced in its place.[3] In Scotland, for some decades prior to 1870, arrestments of wages were especially unpopular[4] until the reforms of that year.[5] Civil imprisonment, never widely used on this side of the border, was virtually abolished in Scotland as a general creditor's diligence in 1880 and in 1882 was made subject to judicial discretion in most of the few cases where it remained competent and was in practice used.[6]

2.145 In recent years, the diligence of poinding and warrant sale has become probably the most unpopular diligence in Scotland as well as being the most frequently used. It is tempting to conclude from this that the diligence can simply be abolished as a humanitarian reform equivalent to the virtual abolition of civil imprisonment and as the logical next step in the progressive development of the law. We think that this temptation should be resisted unless it can be demonstrated that an alternative mode of enforcement can be devised which would be as effective and more socially acceptable. Having considered the matter anxiously and at length, we believe that such an alternative cannot be devised.

2.146 On consultation, those who called for "abolition" of the diligence of poinding and warrant sale do not seem to have contemplated the complete abrogation of the diligence throughout its whole field of application: thus, various qualifications were made such as abolition "as far as the domestic sector is concerned" (Convention of Scottish Local Authorities) or abolition "in respect of domestic/individual debt cases" (Labour Party, Scottish Council). And it may be that a similar restriction was contemplated by the Scottish Association of Citizens Advice Bureaux when, as noted above,[7] they suggested that the diligence should be replaced by a summary bankruptcy procedure.

2.147 To focus the true issues, therefore, certain irrelevant considerations must be set aside. Thus we do not think that those who call for abolition of the diligence of poinding and warrant sale are seeking to argue for the abolition of diligence against all moveable goods as such. There has never, we think, been any controversy over the propriety of a creditor executing diligence against, say, commercial goods owned by a trader in order to recover

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[1]Administration of Justice Act 1970, s. 11.

[2]Wages Attachment Abolition Act 1870.

[3]Administration of Justice Act 1970, ss. 13–28, re-enacted in the Attachment of Earnings Act 1971.

[4]See McKechnie Report, paras. 66–76 for the history of limitation: see also D. Englendar, "Wage arrestment in Victorian Scotland" (1981) 60 Scottish Historical Review 68.

[5]Wages Arrestment Limitation (Scotland) Act 1870.

[6]Debtors (Scotland) Act 1880; Civil Imprisonment (Scotland) Act 1882.

[7]See para. 2.113.

debts from that trader.[1] Moreover, we do not think that an argument for abolition of diligence against moveable goods as a class could be sustained even if it were advanced. As the Hughes Report put it[2] "where the debtor has some resources at his disposal it is obviously important that our system of justice provides a reasonably efficient means for the creditor to gain possession of whatever proportion of them is needed to extinguish the debt". If such procedures were not available in relation to moveable goods, of whatever kind and however great the value, then it seems to us that great inequities would arise not only to creditors but also as between classes of debtors depending upon the character of the assets which they owned and there would be a wholly undesirable temptation to convert funds in bank accounts or other assets so far as possible into corporeal moveable goods (such as luxury goods or collectors' items) in order to put them beyond the reach of creditors.[3]

(ii) *Exemptions for all personal or consumer debts or all household goods?*

2.148 We think that the true issue in reform relates to the extent to which the diligence of poinding and warrant sale should be allowed to be executed against the goods of certain classes of debtor or against certain categories of household goods. Put another way, that issue is concerned with whether the existing exemptions from diligence against moveables (which broadly apply so as to exempt certain essential household goods) should be restated so as to confer exemption on whole categories of debtors (such as consumer debtors) or in respect of whole categories of moveable goods (such as household goods).

2.149 We do not think that a global exemption from diligence against moveables for the benefit of consumer or non-business debtors as a class would be equitable. A global exemption of such a kind would have the same undesirable consequences as exempting moveable goods as a whole from diligence. It would enable a debtor to retain, free from diligence by his creditors, goods of considerable value merely because of the irrelevant accident that his debt happened to be a "consumer" debt. Even a Rolls Royce car, for example, would cease to be poindable for a debt incurred by the owner as an individual or as consumer. A global exemption would also result in unacceptable inequities as between classes of debtor. A commercial debtor, in all cases, would remain subject to the full rigour of diligence in respect of all his goods, including his household goods, whereas a consumer debtor's moveable goods would be creditor-proof however much those goods might be excess to his needs.

2.150 Another legislative option is that all goods in a debtor's dwellinghouse ("household goods" for short) should be exempt from poinding and warrant sale. We do not accept this option. While a person's home may be his castle, we do not think that it should be turned into a sanctuary in which he can

[1]However, the present exemption of "tools of the trade" from diligence does indeed require reform.

[2]Para. 12.2.

[3]It is no answer to say that such goods would be attachable in sequestrations under bankruptcy legislation: exemptions from sequestration and diligence should be the same and it would be nonsensical to require a full sequestration of all assets where only moveable goods were sought to be attached.

collect moveable goods and place them out of the reach of his creditors. A good exemption law should not allow the unscrupulous to evade their creditors' lawful claims.

2.151 The point is sometimes made by those who argue for the exemption of household goods as such from diligence, that diligence against such goods can only be uneconomic from the creditor's point of view, given the likely low resale value of the goods in question. We do not think that this is a good argument for creating an exemption for household goods as a class. As we point out above,[1] the low level of debt recovery under the very small number of warrant sales which actually take place does not at all indicate that the diligence *as a whole* is economically ineffective. The level of recovery at warrant sales (on which the economic inefficiency argument is based) is not a true measure of the efficiency of the diligence. The true measure is the extent to which creditors are able, against the background of the potential threat of a warrant sale, to elicit payment of their debts in the vast majority of cases without recourse to such sales.

2.152 It might be assumed that, given that the final stage of warrant sale is (viewed in isolation) inefficient when applied to household goods but the earlier stages of the diligence relatively effective in eliciting payment, then in diligence against household goods, the final stage of warrant sale should be abolished leaving the earlier stages to operate. This argument, however, overlooks the fact that the earlier stages of a poinding process would be wholly ineffective, and indeed pointless, if the ultimate threat of an eventual sale was not present in the background as a possibility. The whole point of a poinding is to attach goods as a necessary prelude to their eventual compulsory sale if, in the meantime, the debt is not paid.

2.153 Another argument which has been advanced to support abolition of poindings of household goods is that it would put an end to the practice whereby poinding and warrant sale procedures are used to elicit payments from social security benefits which are not themselves liable to diligence in the hands of the department paying the benefit and are intended to be used for the subsistence and maintenance of the debtor and his dependants. We think, however, that the abolition of poindings of household goods in order to frustrate that practice would be an undiscriminating solution since the abolition would apply to all debtors who are at present subjected to poindings, many, perhaps the majority, of whom are not dependent on social security as their main source of income.[2]

(iii) *Outline of recommended reforms (Chapter 5; Bill, Part III)*

2.154 We have concluded therefore that the proper strategy for reforming dilligence against moveable goods is not to introduce undiscriminating

[1]Para. 2.49.

[2]Edinburgh University Debtors Survey, para. 2.4 found that of 100 debtors subjected to diligence who were interviewed, the number of debtors out of work at the time when credit was extended was 25; at the time of the summons in the court action 58; and at the time of the interview (soon after the execution of various steps in diligence) 37. For defenders in court actions, see para. 2.64 above: at the time of the debt or debt-related action, 55% of defenders were in full-time employment, and in 59% of defenders' households social security was *not* the main source of income.

legislation abolishing the diligence or exempting all consumer debtors or all household goods from its operation but rather to reform the diligence so that its impact on debtors is made as humane as is possible consistently with the need to retain the effectiveness of the diligence as a method of eliciting payment from debtors who can, but will not, pay their debts. In formulating detailed reforms, we have sought to strike a proper balance between the interests of debtors and creditors and while we concede that we have found that task to be extremely difficult, we are firmly of opinion that the strategy itself is right.

2.155 We propose that the main features of the reformed diligence would be as follows.

(1) The diligence would continue to take the form of an attachment followed by a sale arranged by an officer of court under the supervision of the sheriff and the main stages of the diligence (the charge, the poinding, the grant of warrant of sale on the creditor's application and the sale itself) would be retained. We envisage that the diligence would continue to have a filter effect such as we described above and indeed the additional safeguards suggested below would be likely to result in even fewer cases reaching the stage of warrant sale than the tiny percentage under the present law. Despite these safeguards, we think that the diligence would continue to be a credible sanction against debtors able to pay their debts.

(2) The charge would be retained as a means of notifying the debtor of the decree, of warning him that poinding may follow in default of payment and of informing him of his new rights to apply for a time to pay order or a debt arrangement scheme. We envisage that the service of a charge would continue to be a valuable catalyst for payment arrangements and a means of enabling sheriff officers to report to creditors on the prospects of recovery.
(Paragraph 5.9; clause 115(1)).

(3) We believe that creditors should continue to be entitled to ascertain the extent of the debtor's poindable goods and this necessarily implies that officers of court executing a poinding should retain their power of entry to the debtor's premises, by force if necessary. But officers of court should not be entitled to enter empty houses or houses with unattended children under 16 unless prior notice of intended entry had been given to the debtor and, in the case of unattended children, the director of social work or unless the sheriff's authorisation had been obtained.
(Paragraph 5.85; clause 45).

(4) The exemptions from poinding of household goods and certain other goods should be codified by statute, capable of amendment by statutory instrument, and the range of exempt goods should be extended to cover, among other things, all items reasonably required for the use of the debtor and the members of his household.
(Paragraphs 5.48, 5.51 and 5.57; clause 43(1) and (2)).

(5) As under the present law, poinded goods should normally remain in the debtor's possession unless and until, at a later stage in the

procedure, (which in the great majority of cases is not likely to be reached), the goods have to be removed for sale.
(Paragraph 5.95; Recommendation 5.19(1)(i); clause 46(1)(*g*)).

(6) After the poinding, the debtor would retain his existing right to apply to the sheriff for the release of exempt goods and have a new right to apply for the release of individual items on the ground of undue harshness.[1] He would have a much longer period than under the present law to redeem goods at their appraised values, and a second chance of redemption if the creditor applied for warrant of sale.
(Paragraphs 5.65, 5.95 and 5.150; clauses 43(4), 46(5), 48(1) and 53(2)).

(7) At any time after a poinding and before the creditor applied for warrant of sale, the debtor would have an important new right to apply to the sheriff for recall of the poinding on the ground that the eventual grant of warrant of sale would be unduly harsh; or that the valuations of the poinded goods made by the officer executing the poinding (which fix the minimum amounts credited to the debtor for the goods if they are sold or transferred to the creditor in default of sale) were substantially below the aggregate market values; or that the likely proceeds of sale would not be likely to cover the expenses incurred in applying for warrant of sale and in completing the diligence. We envisage that these would also be the grounds on which the sheriff could refuse to grant warrant of sale at the later stage when the creditor applies for such a warrant. Thus in cases where warrant of sale would not be granted, the debtor need not remain under the uncertain threat of a sale but could have the poinding recalled. Recall of the poinding would also be competent on the ground that the poinding was invalid or had ceased to have effect (e.g. if the debt had already been paid).
(Paragraphs 5.137 and 5.146; clauses 49(1) and (2) and 52(1) and (2)).

(8) The debtor would also have a new right to be informed of the creditor's application to the sheriff for warrant of sale, and an opportunity of intervening to oppose the application on any of the grounds mentioned above.
(Paragraph 5.146; clause 52(3) and (4)).

(9) The research discloses that debtors dislike and indeed fear newspaper advertisements of sales in the home even more than the sale itself, and the problem of low prices at warrant sales is well known. We therefore propose, on social grounds and to secure so far as possible better prices, that warrant sales of goods poinded in a debtor's or other person's dwelling should take place in an auction room rather than in the dwelling. Sales in a dwelling would be permitted only if the occupier, and if he is not the occupier, the debtor, had consented in writing. Public notices of warrant sales would not identify the debtor unless the sale was, with his consent, to be held in his premises. As a result of these important reforms, separate newspaper advertisements publicising sales of household goods and identifying the debtor would be virtually abolished and the sale itself would be a less painful

[1]The release of goods from a poinding would not bring the whole poinding to an end unless all the goods were released. Release is thus to be contrasted with recall of a poinding which always terminates the whole diligence.

experience for debtors.
(Paragraphs 5.161 and 5.166; clauses 54(2)–(4) and 56(5)).

(10) To ensure that debtors would not remain perpetually under threat of poinding for a particular debt, the present restriction on second poindings on the same premises for the same debt imposed by Practice Notes of the sheriffs principal would be enacted in statutory form.
(Paragraph 5.134; clause 50).

(11) To enable informal instalment arrangements secured by poinding to be made providing for smaller amounts than are possible under the present practice, a period of one year (instead of six months, as at present) between the poinding and the application for warrant of sale would be allowed, subject to extension by the sheriff on cause shown.
(Paragraph 5.130; clause 62(1) and (2)).

(12) Following the grant of warrant of sale, the creditor would be entitled to cancel arrangements for the sale and make an instalment arrangement secured by an extension of the poinding but, to prevent the diligence from continuing indefinitely, this would be possible on one occasion only and the extension would be limited in time.
(Paragraph 5.197; clause 58).

(13) Provision would be made to ensure that creditors to whom poinded goods are transferred in default of sale could not use the threat of uplifting them as a means of putting further pressure on debtors to pay.
(Paragraph 5.203; clause 59(5) and (6)).

We would again emphasise that the forms served on debtors should be in simple language prescribed by rules of court with a view to making them more informative and intelligible to ordinary people. We discuss these reforms in greater detail in Chapter 5 together with other amendments of the law which we have found it necessary to recommend.

2.156 We do not claim that our recommended reforms will meet all the criticisms which have been made of poinding and warrant sale procedures. Such reforms will not satisfy those who believe that a system of enforcing debts without coercion is practicable. Moreover, we concede that if insolvent debtors do not apply for the various orders safeguarding them from diligence, or do not comply with payment arrangements made in orders controlling diligence, then the burden of the original debt will often be increased by the additional burden of diligence expenses. In some cases this burden, already regarded as heavy relative to debts of small amount, will actually be increased by our recommendations, as where goods have to be removed to an auction room. We revert below to the problems of diligence expenses, some of which appear to be well nigh intractable. Only experience will tell precisely how far the abolition of sales in debtors' homes and the relative advertisements will lessen the effectiveness of the diligence from the standpoint of creditors, but the sanction of sale would still exist as a powerful inducement to payment.

2.157 Overall we believe that our recommended reforms of the diligence, taken together with the new discretionary orders controlling diligence described above, should meet the legitimate criticisms of the diligence while by and large preserving its effectiveness as a sanction inducing payment of debts.

(iv) *Restriction on poinding by arresting creditor?*

2.158 Before turning to summarise our main recommendations for introducing a system of continuous diligence against earnings, we would mention a suggestion put to us on consultation by the Tory Reform Group in Scotland that in cases where such a continuous diligence against earnings was in operation, a poinding and sale of "personal assets" of the debtor should not be permitted. After careful consideration, we think that this proposal should not be accepted. There may well be cases where a debtor, whose earnings have been arrested, also holds non-exempt household goods of high resale value, and we do not see why the laying of an earnings arrestment should debar the creditor from poinding those goods. An undiscriminating prohibition of that kind might confer an inappropriate benefit on undeserving debtors. Generally speaking, under the present law, a creditor who has ascertained the name and address of the debtor's employer will use a wages arrestment alone and will not have recourse to a poinding unless the creditor has good reason to do so.[1] We would expect that practice to continue, but in cases where a poinding is indeed executed while earnings were being arrested, the debtor would, we believe, be sufficiently protected by the reforms which we have already outlined.

(b) Reform of diligence against earnings (Chapter 6; Bill, Part IV)

2.159 Apart from poinding and warrant sale procedures, the other method of enforcing payment of debts considered in this report is the use of arrestments against an individual's earnings.[2] While arrestments of earnings have not in recent years attracted the same degree of public criticism and controversy as poindings and warrant sales, there was widespread agreement on consultation with the view stated in our Consultative Memorandum No. 49 that the diligence should be radically reformed. Our proposed reforms seek to improve the efficiency of arrestments of earnings from the creditor's point of view while at the same time ensuring so far as practicable that the amount to be deducted from the debtor's earnings is not such as to impose undue hardship on him.

2.160 An arrestment of earnings operates at present to attach a debtor's earnings only for the single pay period in which the arrestment is served, and

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[1]See C.R.U. Creditors Survey, para. 1.15: "Creditors generally prefer to instruct the arrestment of a debtor's wages or salary rather than charge, poinding and warrant sale procedures because an arrestment secures at least some of the money due directly, rather than relying on the threat of a warrant sale securing payment indirectly": See also paras. 6.10 and 6.11. This is a traditional viewpoint. See the Hill Burton Report of 1854 which observed that poinding is "ever surrounded by unpleasant circumstances" and "is a much more protracted, expensive and cumbrous process than arrestment". Arrestment, according to the Report "is easy and systematic. It is a method of drawing off a portion of the workman's supplies ere they reach himself. It makes the creditor a participator in the income of the debtor; and in point of ease in operation between it and other methods of recovery, there is all the difference that there is between the interception of money before it comes into possession and its seizure after it has come into possession". Parliamentary Papers (1845) LXIX, p.41. Some debt collection agencies instruct a charge and then decide on whether to poind or arrest; C.R.U. Creditors Survey, para. 6.11

[2]For the reasons given at para. 2.4 above, we are not concerned in this report with the reform of arrestments used against moveable goods and funds other than earnings in the hands of the debtor's employer.

does not affect earnings for any subsequent pay period. This gives rise to two major defects in the operation of the diligence, namely:

(1) repeated arrestments (for the expenses of which the debtor will be liable) may be needed to clear a debt unless an instalment settlement can be reached or unless the creditor abandons recovery;

and

(2) the proportion of an individual's earnings in any pay period which are exempt from arrestment for an ordinary debt[1] (reflecting, as it does, the present inability of the creditor to arrest the earnings for more than a single pay period) is too low and leaves debtors with insufficient means on which to subsist. In the case of an arrestment enforcing maintenance, the whole earnings for the relevant pay period are attached leaving the debtor with nothing.

There was general agreement on consultation with our view that, in order to cure these defects, a system of continuous diligence against earnings should be introduced which would avoid or minimise the need for repeated arrestments but would leave the debtor with sufficient for subsistence. In Chapter 6, therefore, we advance detailed proposals for the introduction of such a system. In summary, the proposed system is as follows.

(i) *Earnings arrestments*

2.161 In our Consultative Memorandum No. 49, we sought views on whether the system of continuous diligence should take the form of an arrestment in which the deductions from earnings are fixed by legal rules which would be applied by the employer, or whether the system should follow the pattern of the English attachment of earnings orders in which the court has a discretionary power to fix the level of deductions after an enquiry into the debtor's means. The fact that arrestments can be used without the trouble and expense of a court application and a compulsory means enquiry is a great advantage, and probably explains why creditors in Scotland use enforcement against earnings instead of enforcement against moveable goods considerably more than creditors in England do.[2] For this reason, we recommend a system with deductions fixed by legal rules rather than judicial discretion. We envisage that the existing diligence of arrestment and furthcoming should no longer be used against the debtor's earnings in the hands of his employer. Instead, debts would be enforceable by new diligences against earnings. Where the debt was an ordinary debt (i.e. a debt other than current maintenance) the creditor could execute a new diligence called an "earnings arrestment".[3] This would, broadly speaking, require the employer to deduct on each pay day until the debt was cleared the appropriate weekly, monthly or other sum fixed by reference to a statutory table of deductions designed to be as easily operated by employers as is practicable. The deductions would be of relatively small amounts compared with the present law but the amounts would, we believe, be generally fair and would be on a sliding scale increasing with the amount of net earnings, but with a threshold of net earnings below which earnings would be wholly exempt from diligence. No actions of furthcoming

[1]I.e. a debt other than maintenance.

[2]See para. 2.143 above.

[3]See Chapter 6, Section C (paras. 6.31 to 6.130); Bill, clauses 75–78; and Scheds. 2 and 3.

would be necessary and the employer would be bound to deduct the appropriate sum on each pay day and pay it to the creditor forthwith.

(ii) *Current maintenance arrestments*

2.162 The reform of diligence against earnings enforcing maintenance (i.e. periodical allowance on divorce and aliment) presents somewhat different problems from the enforcement of other debts. As indicated above,[1] the focus of public concern has been directed not so much to the protection of defaulting debtors but rather to improving the machinery for the collection, as well as the enforcement, of maintenance. Maintenance creditors—normally separated or former wives, unmarried mothers, and children—are generally more in need of assistance in debt recovery than are most other creditors. On the other hand, arrestments can operate even more harshly against maintenance debtors than against other debtors because an arrestment enforcing maintenance attaches the whole earnings of a debtor on the relevant pay day without any exemption.

2.163 To cater for the special needs of maintenance creditors and the special characteristics of maintenance, we propose that a separate new diligence enforcing maintenance against earnings should be introduced to be called a "current maintenance arrestment".[2] Maintenance differs from other civil debts in so far as the obligation is a continuing one to pay periodic amounts which are fixed by the court at a level designed to reflect the debtor's ability to pay. And the award can be varied or recalled on a material change in circumstances. If the court's assessment of the debtor's ability to pay has been properly made, then—other circumstances remaining unchanged—it would seem right in principle for the whole of the maintenance instalments to be deducted from the maintenance debtor's earnings at source. The new diligence of current maintenance arrestment described in Chapter 6 is designed to achieve that aim, subject again to a threshold below which earnings would be exempt.

2.164 Another significant difference between maintenance and ordinary debts is that maintenance, whether it be periodical allowance or aliment, is designed for the current support or subsistence of the maintenance creditor. If maintenance is to achieve that objective, then, following default, maintenance should in principle be recoverable thereafter as each periodic amount falls due or as nearly thereto as is practicable. Under the existing law, only arrears of maintenance can be attached, and this is understandable given that a single wages arrestment attaches wages only on a single pay day. But if the principle of continuous diligence against earnings is introduced, then, having regard to the objective of maintenance, it seems to us better to prevent arrears arising by attaching current maintenance than to allow maintenance to fall into arrears and to provide for the recovery of the arrears after they have arisen. A current maintenance arrestment therefore, as its name implies, would attach in each pay period the maintenance due in respect of that pay period. We consider that a current maintenance arrestment should be competent once the maintenance debtor defaults, and that the maintenance creditor should be entitled to recover both future maintenance by a current

[1]Para. 1.6.

[2]See Chapter 6, Section D (paras. 6.131 to 6.217).

maintenance arrestment and arrears by an ordinary earnings arrestment operated concurrently or consecutively.

2.165 If current maintenance arrestments are introduced and operate successfully, they may largely solve the main problems of recovering maintenance which led the McKechnie Committee[1] to recommend the introduction of an official system of collection of maintenance in the sheriff courts.

(iii) *Competitions between arresting creditors; conjoined arrestment orders*

2.166 A system of continuous diligence against earnings must provide a solution to the problem of competitions between two or more creditors who use or seek to use earnings arrestments to operate simultaneously against the same debtor's pay. In the absence of such a solution, later creditors would be "shut out" by the first arresting creditor, in many cases for a considerable period, and might resort to poindings instead. A current maintenance arrestment would shut out later arrestments for very long or even indefinite periods, depending on the duration of the maintenance obligation being enforced. We discuss various policy options in Chapter 6. We argue there that, while an employer should be required to operate one earnings arrestment and one current maintenance arrestment simultaneously, in other cases of competitions between creditors, the second or subsequent creditor should apply to the sheriff for an order—which we call a "conjoined arrestment order"—requiring the employer to make deductions from earnings, computed in accordance with the rules on earnings arrestments and current maintenance arrestments as the case may be, and to pay them to the sheriff clerk who would disburse those sums to the competing creditors rateably in proportion to the amount of their debts.[2]

2.167 We concede that this solution would have some resource implications for the sheriff courts but we think it would be neither fair nor practicable to impose on employers, in addition to the burdens which continuous diligence against earnings would in any event entail, the further burden of making disbursements to creditors in proportion to their respective shares.

Diligences and priorities enforcing rates, taxes and Crown debts (Chapter 7; Bill, Part V, Schedules 5 and 6)

2.168 In this report we recommend reforms of diligence enforcing summary warrants for the recovery of rates and taxes, (though we do not consider the procedure for obtaining a summary warrant upon which we have not consulted and express no view). We also propose the abolition of (a) civil imprisonment for non-payment of tax penalties and rates and civil fines and penalties due to the Crown, with minor exceptions (e.g. fines for contempt of court); (b) Exchequer diligences and their concomitant Crown preferences; (c) the priorities of tax and rates arrears arising where moveable property is taken by diligence or assignation from rates or tax defaulters; and (d) the vestigial remains of *fugae* warrants.

2.169 Diligence under summary warrants for recovery of rates and taxes

[1]McKechnie Report, paras. 258–298.

[2]See Chapter 6, Section E (paras. 6.218 to 6.280); Bill, clauses 87–92 and Sched. 4.

differs from ordinary diligence in two main ways: first, there are special forms of poinding under summary warrants for the recovery of rates and taxes and second, tax summary warrants (unlike rates summary warrants) do not authorise arrestments. Summary warrant poindings are not under the automatic supervision of the sheriff and the procedure is therefore simpler than in ordinary poindings; there is no prior charge, no report of poinding, no application for warrant of sale, and no report of sale. In our Consultative Memorandum No. 48,[1] we suggested that the absence of supervision could be justified on the ground that creditors in summary warrant diligence are central or local government departments who ought to be trusted to use their powers of enforcement in a responsible manner and without oppression. On consultation there was no dissent from this view and, moreover, there was general agreement with our proposal[2] that the separate codes on poindings under rates and tax summary warrants should be replaced by a single uniform modern code and that tax summary warrants should authorise arrestments.

2.170 In Chapter 7, therefore, we advance recommendations to achieve those aims. The new uniform summary warrant poinding procedure would confer on rates and tax defaulters the main protections for debtors embodied in the new poinding procedure outlined at para. 2.155 above, including the new rules on exemptions,[3] rights to redeem the goods at appraised values,[4] the judicial powers to release individual items as exempt or on the ground of undue harshness,[5] and the judicial powers to recall the poinding in the case of undue harshness, low valuations or where the expense of a sale would not be justified by its proceeds.[6] New provisions would be introduced to prevent sales in dwellings without the consent of the debtor or occupier and advertisements of sales identifying the debtor unnecessarily.[7] As under the present law, however, the procedure would not be under the automatic supervision of the sheriff and thus there would be no report of poinding, no separate application for warrant of sale and no report of sale. Other useful related reforms include the abolition of the statutory fee (ten per cent of the tax arrears) payable to sheriff officers executing tax warrants which would be replaced by scale fees prescribed by rules of court.[8]

Section G. Officers of court (Chapter 8; Bill, Part VI)

2.171 Officers of court not only hold the public office of messenger-at-arms or sheriff officer but are also independent contractors who receive instructions to execute diligence in much the same way as commercial agents receive instructions from their principals. There are, however, important differences from commercial agents: for example, an officer of court has a duty to execute diligence when instructed and cannot pick and choose as between instructing creditors; his fees for executing diligence are prescribed in detail by rules of court; and as a sheriff officer he is subject to the disciplinary authority of the

[1]Para. 7.8.
[2]Consultative Memoranda No. 48, paras. 7.9 and 7.21 and No. 49, para. 4.18.
[3]Bill, Sched. 6, para. 1.
[4]Recommendation 7.6(1) and (2) (para. 7.30); Bill, Sched. 6, paras. 5(5) and 11(2).
[5]Recommendation 7.8 (para. 7.39); Bill, Sched. 6, para. 6.
[6]Recommendations 7.6(3) (para. 7.30) and 7.8 (para. 7.39); Bill, Sched. 6, para. 7(2).
[7]Bill, Sched. 6, paras. 10 and 12(4).
[8]Recommendation 7.14(1) (para. 7.61); Bill, Sched. 5, paras. 1, 2, 6 and 7.

sheriff principal (or of the Lyon King of Arms in the case of messengers-at-arms) for fault in the performance of his official functions.[1] This independent contractor status cannot be accurately regarded either as peculiarly Scottish or an anachronism; the enforcement officers of the French courts (the *huissiers*) and of the English High Court (the sheriff's officers) for example are also independent contractors.

2.172 On consultation most of those who expressed a view considered that the existing system of independent contractor officers should not be replaced by a system of salaried officers employed within the Scottish Court Service but rather that improvements should be made to the existing arrangements for the regulation, supervision and control of independent contractor officers. Our own view is that, while the existing system has its defects as any system would, it has also many merits and has served Scotland well. We think that independent contractors are likely to give a more efficient service at less cost than a system of salaried officers.

2.173 For these reasons, we conclude that the existing system of independent contractor officers should be reformed rather than abolished. In Chapter 8, therefore, we advance recommendations for improvement of the arrangements for the regulation, appointment, training, supervision, control and discipline of officers of court. We envisage that (as is broadly the present practice) each court or group of courts should appoint, supervise, discipline and control the officers who execute its decrees. Public confidence in the system demands that officers of court holding a public office and possessing powers of forcible entry should be, and should be seen to be, accountable to the courts. The reformed system therefore would not leave sheriffs principal merely to react to complaints against sheriff officers from debtors or other members of the public, but would enable sheriffs principal, of their own accord, to order the inspection of the work of officers.[2] In addition sheriffs principal would have new powers to initiate formal procedures for disciplining sheriff officers.[3] The Court of Session would have similar powers in relation to messengers-at-arms.

2.174 Following public concern as to the role of officers of court in debt collection and in the enforcement of debts due to bodies in which they have an interest, we advance recommendations, which were generally approved on consultation by those who commented, on these matters. The rule precluding an officer of court from enforcing a debt due to himself would be extended to enforcement on behalf of members of his family and business associates and of firms in which he or they have a controlling interest.[4] As regards collection of debts for remuneration, we think that the Court of Session should make rules prohibiting officers from purporting to act as such in collecting debts before decree,[5] and making collection after decree an official function guaranteed by the officer's bond of caution.[6] Whether collection of debts through a debt collection agency in which the officer enforcing the debt has an interest is incompatible with the officer's official functions will depend

[1]See generally Chapter 8 below.
[2]Recommendation 8.10 (para. 8.66); clause 104.
[3]Recommendation 8.12 (para. 8.84); clauses 105 and 106.
[4]Recommendations 8.16, 8.17 and 8.18 (paras. 8.96, 8.100 and 8.104); clause 109.
[5]Recommendation 8.20 (para. 8.113); clause 101(1).
[6]Recommendation 8.22 (para. 8.125); clause 101(1).

on the circumstances of each case. Flexible provision seems necessary and we envisage that this and other extra-official activities undertaken for remuneration could be regulated by rules made by the Court of Session and if not so regulated the sheriff principal's permission would be required in particular cases.[1]

Section H. Other reforms (Chapter 9; Bill, Parts VII and VIII)

2.175 In accordance with our statutory functions of simplification and modernisation of the law, we have taken the opportunity afforded by this report of making recommendations to modernise the law on the grant of warrants for diligence,[2] to abolish obsolete procedures (such as the grant of signeted letters of horning, poinding and caption),[3] to repeal most of the Debtors (Scotland) Act 1838 and many out-of-date pre-Union Acts;[4] and to complete the trend towards making warrants of concurrence for the execution of diligence unnecessary.[5]

Expenses of diligence

2.176 We referred above[6] to the fact that the burden of the original debt falling on a debtor may be considerably increased by the further burden of the court and diligence expenses incurred in its enforcement. Though we reviewed the system of charging fees in some detail in our Consultative Memorandum No. 47,[7] we received no evidence that the fees of officers of court are too high, viewed as remuneration for work done. There seems no scope for reducing the burden of diligence expenses falling on creditors and debtors by reducing the fees exigible for diligence, and any change in the basis of charging fees (e.g. with respect to mileage charges) would simply mean that some parts of the work (e.g. enforcement in populous areas) would subsidise other parts (e.g. enforcement in remote areas). The only alternative would be a public subsidy, an approach which we regard as falling outside the scope of this report and on which we express no view.[8]

2.177 We think that creditors must be entitled to recover the expenses of diligence from debtors, especially having regard to the fact that debtors will now have ample opportunity to obtain orders giving them time to pay by reasonable instalments before diligence expenses have ever been incurred. We think, however, that creditors should only be entitled to recover the expenses of a particular diligence[9] from the fruits of that diligence or from payments made by the debtor to the creditor while it is in operation: they should generally not be entitled to recover those expenses by means of another

[1]Recommendations 8.19 and 8.21 (paras. 8.110 and 8.121); clause 101(1) to (3).
[2]Recommendations 9.1 (para. 9.7) and 9.2(2); clauses 112, 113 and Sched. 7, paras. 8 and 10.
[3]Recommendation 9.2(1); clause 114.
[4]Bill, Sched. 9.
[5]Recommendation 9.5 (para. 9.26); clause 116.
[6]See para. 2.70.
[7]Paras. 3.19 to 3.52.
[8]A public subsidy system for diligence in the remote areas was introduced by the Remote Areas Diligence Payments Scheme of 1959 which was a total failure. We did not receive much evidence that enforcement in the remote areas now presents especially difficult problems, perhaps because of improved means of transport.
[9]I.e. poinding and sale; earnings arrestment; application for the making of, or for inclusion in, a conjoined arrestment order; arrestment and furthcoming.

diligence under the same decree or (as under the present law) by means of a subsequent decree authorising further diligence to recover those expenses.[1] Thus, while a creditor should be allowed to ascertain the extent of his debtor's poindable effects, and to recover the expenses out of the proceeds of sale or an instalment arrangement, he will also take the risk that the diligence may be abortive. Debtors wishing to stop a diligence will have to tender diligence expenses so far incurred as well as the principal sum,[2] but will not be subjected to further proceedings for expenses after the diligence is terminated. We envisage that forms served on debtors should show the state of the debt and to facilitate the calculation of expenses chargeable against debtors, the legislation should so far as practicable specify the steps of diligence so chargeable in detail.[3] We think that these reforms would achieve a fair balance between the interests of creditors and debtors.

[1]Recommendation 9.9 (para. 9.58); clauses 118 and 119.
[2]Recommendation 9.9(4) (para. 9.58); clause 120.
[3]See Recommendation 9.7 (para. 9.36); clause 70 and Sched. 1; also Sched. 6, paras. 25–33.

CHAPTER 3

TIME TO PAY DECREES AND ORDERS

Preliminary

3.1 In Chapter 2, we set out the reasons of principle which led us to recommend the introduction of discretionary court orders giving debtors an extension of time for payment of their debts. In this Chapter we set out our detailed proposals on two of these types of order, namely, time to pay decrees which would be available when decree is granted in court proceedings and time to pay orders which would be granted by the court at a later stage in the debt recovery process.[1]

Section A. Time to pay decrees

Introduction of time to pay decrees

3.2 Under the present law, the defender in a sheriff court summary cause action may apply for what is generally known as an instalment decree allowing him time to pay the debt, or the expenses of the action, by instalments rather than an "open" decree requiring payment of the whole debt in one lump sum.[2] The creditor cannot execute diligence to enforce the debt or other sum unless the debtor allows an instalment to remain unpaid until the next falls due, i.e. default on two instalments.[3] On such default, the right to pay by instalments lapses automatically and the decree is converted into an open decree enforceable by diligence. We propose that this system of instalment decrees should be replaced by time to pay decrees which would be available in Court of Session actions and sheriff court ordinary cause actions, as well as sheriff court summary causes. While time to pay decrees would have many of the same characteristics as summary cause instalment decrees, (e.g. as to the principle of automatic lapse on default), there would be some significant differences which we describe below.

3.3 *Instalments and deferred lump sums.* The sheriff's power in summary causes appears to be limited to a power to direct payment of the debt by instalments.[4] In some cases, however, it may be appropriate that the debtor should pay the whole debt in a lump sum after a breathing space of such period as the court may fix in the decree, for example when it is known that the debtor will come into funds at a certain time in the future. We think that the restriction in the present law makes the power unnecessarily inflexible and that time to pay decrees for payment by a deferred lump sum should be possible.

3.4 We **recommend:**

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[1]The other main type of order—an order confirming a debt arrangement scheme—is discussed in Chapter 4.

[2]Sheriff Courts (Scotland) Act 1971, s. 36(4): see paras. 2.26 and 2.27 above.

[3]Summary Cause Rules, Form U2.

[4]Sheriff Courts (Scotland) Act 1971, s. 36(4). The sheriff may attach conditions, including presumably a condition delaying the commencement of the instalments though such a condition seems to be unusual.

The present jurisdiction of the courts to grant instalment decrees in summary cause actions should be replaced by a jurisdiction to grant decrees containing directions (called time to pay directions[1]) providing for payment of the debt by instalments or by a deferred lump sum.
(Recommendation 3.1; clause 1(1).)

Who may obtain a time to pay decree?

3.5 We envisage that the right to apply for a time to pay direction should be available to any individual who is a party to an action or other court proceeding and against whom a decree for payment of a sum of money is pronounced including for example a pursuer held liable in a counterclaim and a third party minuter.

3.6 Although the existing power in summary causes is not expressly confined to decrees against individuals (i.e. natural persons),[2] it seems likely that the power is rarely, if ever, exercised in favour of companies or other bodies corporate. On consultation,[3] it was generally agreed that title to apply should not extend to bodies corporate and we adhere to that view.

3.7 Clearly individuals who are personally liable for payment under the decree should have a title to apply for a time to pay direction. Where an individual is found liable by the decree in a representative or fiduciary capacity only, and not in a personal capacity (e.g. trustees under trust deeds, executors, trustees in bankruptcy sequestrations, or the office bearers or representatives of a club or other voluntary association, who are found liable as such), we think that, as a general rule, that individual should not have a title to apply, and that diligence should proceed against the assets of the trust, association or other body in the ordinary way. An exception should, however, be made in favour of persons held liable in a representative or fiduciary capacity as a tutor of a pupil child or of another individual,[4] a judicial factor *loco tutoris*, a curator *bonis* (i.e. a judicial factor managing the estate of a minor or of an adult incapable of managing his affairs) and a judicial factor *loco absentis* on the estate of a missing person. Here the tutor or judicial factor merely stands in the place of his ward. Judicial factors can be appointed in many other contexts,[5] which cannot be exhaustively defined, but the inclusion of further categories would either be inappropriate[6] or require over-elaborate statutory provision to cater for an insignificant number of cases.

3.8 An individual may be found liable under a decree either in a personal capacity or in a representative or fiduciary capacity or in both capacities. Normally the express terms of the decree will make it clear in what capacity

[1]For brevity, in this report we refer to a decree containing a time to pay direction as a time to pay decree.

[2]Sheriff Courts (Scotland) Act 1971, s. 36(4).

[3]Consultative Memorandum No. 48, Proposition 1(6)(*a*) (para. 1.26).

[4]It is still competent for a tutor-dative to be appointed to an adult incapax where it is clear that personal guardianship is required (see e.g. *Dick* v. *Douglas* 1924 S.C. 787) though such appointments are very unusual.

[5]E.g. on a bankrupt's estate under bankruptcy legislation, on a partnership estate, on a fund pending settlement of a dispute by litigation or agreement.

[6]E.g. in the case of judicial factors appointed under bankruptcy legislation or under the Solicitors (Scotland) Act 1980, s. 41.

the defender is found liable. There are special rules, however, applying to decrees against partnerships (which in Scotland have a species of legal personality separate from those of the individual partners) e.g. a firm with a social name[1] may be sued in that name without specifying the names of the individual partners and decree in the action is a warrant to charge either the firm or each of the partners individually,[2] and for diligence against the estate of the partnership and the estate of each individual partner. The rules regulating procedure in the sheriff court also provide that any person or persons carrying on business under a trading or descriptive name may sue or be sued in that trading or descriptive name alone and that an extract of a decree or registered document of debt is a valid warrant for diligence against that person or those persons.[3] This rule covers clubs and voluntary associations as well as partnerships. However, because of judicial dicta in an Inner House case,[4] the practice is to conjoin the names of individuals with the trading or descriptive name. In cases where an individual is liable under a decree of any of these kinds both in a personal and in a representative or fiduciary capacity, we propose that the court should be empowered to include in the decree a time to pay direction applying to the individual's personal obligation only.[5] The practical result would be that, during the period when the time to pay direction had effect, the extract decree would be a warrant for diligence only against the estate of the trust, partnership, association or other person or body for whom the individual acts and not against the individual's own income or assets; and a charge served in pursuance of the decree during that period would require payment to be made by the individual in his representative or fiduciary capacity only and not from his own pocket. Finally, we think it should be made clear by statute that a time to pay direction is personal to the debtor and that the privilege of time to pay would cease to have effect on the transmission *inter vivos* or *mortis causa* to a third party of the debtor's liability to pay the debt.

3.9 We **recommend:**

(1) Title to apply for a time to pay direction should be conferred on a debtor who is an individual and who is either (a) personally liable under the decree or (b) liable in a fiduciary or representative capacity as tutor of an individual or as judicial factor *loco tutoris*, curator *bonis* or judicial factor *loco absentis* on an individual's property.

(2) Where an individual is liable to make payments under a decree both in a personal capacity and in a fiduciary or representative capacity, (e.g. as a trustee, executor or office-bearer of a voluntary association) it should be competent for the court to include in the decree a time to pay direction applying to the individual's personal liability, but not to

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[1]A "social name" is a name using the name or names of persons (e.g. "Brown, Smith & Co") though not necessarily the names of the partners and is to be contrasted with a "descriptive name" which does not contain the names of persons (e.g. "Blackacre Hiring Co").

[2]Graham Stewart, pp. 296 *et seq*. In the case of a firm with a descriptive name, the names of at least three partners must be specified in the summons and decree.

[3]Ordinary Cause Rules, rule 14(1), applied to summary causes by Act of Sederunt (Summary Cause Rules, Sheriff Court) 1976, section 3(2) (as amended).

[4]*Aitchison* v. *McDonald* 1911 S.C. 174 in which it was observed (at p. 175) that "a decree against A is not warrant for a charge against B".

[5]Unless the individual is liable as tutor or judicial factor as mentioned in para. 3.7 above.

his liability in his other capacity unless that other capacity is one of those mentioned in paragraph (1)(b) above.

(3) A time to pay direction should cease to have effect on the debtor's death or on the *inter vivos* transmission of his obligation to pay the debt.

(Recommendation 3.2; clause 12.)

Actions for payment in Court of Session or sheriff court

3.10 The Sheriff Courts (Scotland) Act 1971, section 36(4) seems to have contemplated that instalment decrees would be competent in all types of summary cause action whether the main crave is for payment of a principal sum, or for performance of a non-monetary obligation (such as delivery or removing) in which the only monetary award in the decree is an award of expenses.[1] In practice, instalment decrees seem to be granted only in summary cause actions for payment of a principal sum, perhaps because it is only in such actions that the Summary Cause Rules provide a special procedure for offers to pay by instalments.[2] We propose that, subject to a monetary limit discussed below, the power to grant time to pay directions should be available whenever the court pronounces decree for a principal sum of money, whether the decree is granted in the Court of Session or the sheriff court. A proposal on these lines was generally approved on consultation by those who commented on it.[3] We revert later to awards of expenses in proceedings other than actions for payment of a principal sum.

3.11 We consider that awards of financial provision (capital sums or periodical allowance) on divorce (and on decree of declarator of nullity of marriage if financial provision becomes competent in such decrees[4]) and awards of aliment, whether in actions for divorce or aliment, should be excluded from the time to pay jurisdiction. These awards are in any event based on the court's assessment of the debtor's ability to pay and provisions for the variation and recall of such awards (other than capital sums) already exist: to superimpose a time to pay jurisdiction on these existing provisions would be both unnecessary and undesirable. Decrees for the recovery of the cost of supplementary benefit[5] and contribution orders against relatives liable to aliment a child maintained by a local authority under child care legislation[6] closely resemble awards of aliment and should also be excluded.[7]

3.12 Taxes, fines and penalties due to the Crown and, to a lesser extent local

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[1]This seems to have been a deliberate departure from the former small debt procedure in which instalment decrees for payment of expenses were apparently not competent: see *Archer's Trs.* v. *Alexander and Sons* (1910) 27 Sh.Ct.Reps. 11. Section 36(4) of the 1971 Act expressly mentions expenses.

[2]See Summary Cause Rules, rules 52 and 54; see also Form Q introduced by rule 50A (service document).

[3]Consultative Memorandum No. 48, Proposition 1(7) (para. 1.26).

[4]See the recommendation to that effect in our *Report on Aliment and Financial Provision* (1981) (Scot. Law Com. No. 67), paras. 3.201 to 3.203, now proposed to be implemented by the Family Law (Scotland) Bill 1984 clause 17.

[5]Supplementary Benefits Act 1976, ss. 18 and 19.

[6]Social Work (Scotland) Act 1968, ss. 80 and 81; Guardianship Act 1973, s. 11(3).

[7]Such decrees and orders provide for periodic payments based on the liable relative's ability to pay and are subject to variation by the court.

rates, have traditionally been given a specially privileged position in the law of debt enforcement and bankruptcy e.g. as regards (1) civil imprisonment for debt;[1] (2) the special privileges accorded to Exchequer diligence in competitions with ordinary creditors' diligences;[2] (3) the priority for tax and rates arrears where an ordinary creditor executes diligence against moveables;[3] and (4) preferences in bankruptcy sequestration.[4] In this report we recommend the abolition of (1), (2) and (3).[5] Consistently with these recommendations and the recommendation made below[6] that time to pay orders should apply to rates and tax arrears being recovered by summary warrant diligence, we consider that the above categories of "public" debt should not be excluded from time to pay decrees.

3.13 We **recommend:**

(1) Subject to the monetary limit proposed in Recommendation 3.6 (para. 3.25), time to pay decrees should be competent not only in sheriff court summary cause actions for payment of a principal sum but also in other actions in the sheriff court or Court of Session for payment of a principal sum.

(2) Time to pay decrees should not be competent, however, where:

(*a*) the sum due under the decree consists of or includes an award of financial provision on divorce or aliment; or

(*b*) the decree provides for the recovery by periodic payments of the cost of supplementary benefit from a relative liable to maintain the recipient of the benefit or is a contribution order or similar order against the relative of a child in the care of a local authority.

(Recommendation 3.3; clause 1(1), (4)(*b*) and (*c*), and (7).)

Interest

3.14 Court of Session and sheriff court decrees for payment of a principal sum bearing interest normally require the debtor to pay the principal sum with interest at the specified rate from the date when the interest began to accrue until the debt is paid.[7] Interest accruing before decree is generally not quantified and specified in the decree. In summary cause instalment decrees, the same practice is adopted, the only difference being that the decree directs that payment of interest as well as the principal sum is to be made by instalments of specified amounts.[8] Interest accrues on a daily basis and, because of the complex calculations involved, most debtors are unable to compute it. There is no duty on creditors holding summary cause instalment decrees to intimate a claim for interest in time to ensure that the interest can be paid by the specified instalments. On the other hand, it seems likely that in practice

[1]Debtors (Scotland) Act 1880, s. 4; Civil Imprisonment (Scotland) Act 1882, s. 5; Local Government (Scotland) Act 1947, s. 247(5).

[2]Exchequer Court (Scotland) Act 1856, ss. 30 and 42.

[3]Local Government (Scotland) Act 1947, s. 248; Taxes Management Act 1970, s. 64.

[4]See our Report on Bankruptcy, Chapter 15, and para. 4.84 below.

[5]See Chapter 7.

[6]Para. 3.58.

[7]R.C. Form 2(1); Dobie, *Sheriff Court Styles* pp. 3, 357 and 358; Wilson, *The Law of Scotland Relating to Debt*, pp. 154–7.

[8]Summary Cause Rules, Form U2.

creditors holding summary cause instalment decrees frequently do not claim interest.

3.15 If, as we recommend, larger amounts become payable by instalments or deferred lump sum under time to pay decrees,[1] then more creditors would be likely to claim such interest. Further the interest claimed may amount to a significant sum which ought to be payable by instalments. Since in most cases the creditor would be better placed to calculate that sum than the debtor, we think that provision should be made requiring that a creditor seeking interest which had not been specified as a quantified sum in the decree should intimate its amount to the debtor timeously, failing which he would lose the right to claim interest.

3.16 We **recommend:**

A creditor in a time to pay decree should be entitled to claim interest not quantified in the decree only if he intimates the amount of interest claimed to the debtor not later than a date prescribed by act of sederunt occurring before the date when payment of the last instalment or of the deferred lump sum falls due.
(Recommendation 3.4; clause 1(5).)

Expenses

3.17 *Decrees for payment of principal sum.* In a sheriff court summary cause action, final decree disposing of the action is not granted until the liability of one party for another party's expenses has been determined and the amount of those expenses has been either agreed by the parties or fixed by the sheriff clerk and approved by the sheriff.[2] In the case of a summary cause instalment decree, the sheriff pronounces one decree containing an instalment direction applying both to the principal sum and expenses.

3.18 If, as we propose, however, time to pay directions become competent in actions for payment brought as ordinary causes (as well as summary causes) in the sheriff court and in Court of Session actions for payment, the problem arises that in a significant proportion of those actions a decree decerning for a principal sum and finding expenses due may be extracted some considerable time before the decree for payment of the expenses is extracted.[3] Thus, in the Court of Session, the court pronounces decree for payment of the principal sum together with a finding as to liability for expenses and at the same time,

[1]The summary cause limit is £1,000 of principal sum (exclusive of interest and expenses) whereas the time to pay decree limit which we recommended below is £10,000 (exclusive of interest and expenses).

[2]Summary Cause Rules, rules 87 and 88.

[3]In dealing with expenses, the court has to take two steps which are technically distinct and may be taken at the same time or on different occasions. First, if a party has applied for a decree for expenses, the court must make a finding as to liability for expenses (and this must be made in or before the final decree disposing of the proceedings unless any question of liability for expenses has been expressly reserved for subsequent determination by the court). Second, if expenses are found to be due, the court must grant decree for payment of those expenses. It is the decree (in the technical sense of a decerniture) for payment of expenses, not the finding as to liability, which is the operative part of the court's interlocutor, and it is the decree, not the finding, of which an extract bearing a warrant for diligence is issued. See Lees, *Notes on the Structure of Interlocutors* (1915) pp. 32 and 33.

unless special cause is shown for not doing so, decerns, in a separate interlocutor, for payment of the expenses as they will be taxed by the Auditor of Court.[1] The decree for expenses is not extracted, however, until the expenses have been taxed; the extract of the decree for expenses will then set out the taxed amount of expenses. In defended sheriff court ordinary causes, the court normally grants decree finding expenses due and only at a later stage grants a separate decree for payment of those expenses after the expenses have been taxed by the auditor of court.[2] Thus one action for payment often results in the issue at different times of two extract decrees for payment, one for the principal sum and one for expenses, each separately enforceable by diligence.

3.19 We think that the court should normally be required to exercise its discretion to make a time to pay direction on one occasion only during a court action for payment of a principal sum and accordingly it should only be entitled to grant a time to pay direction in respect of expenses at the time when it grants a decree making a finding of liability for expenses (whether or not that decree also decerns for payment of the expenses). The procedure for taxing expenses and obtaining or extracting a decree for payment of expenses should not be disrupted by an application for a time to pay direction which could have been made at the stage when the court found expenses due. In the great majority of cases where there is liability for both a principal sum and for expenses, this proposal would mean that a time to pay direction would deal with both at the same time. Where the court did not make a direction covering expenses (e.g. where the amount of expenses was difficult to forecast), we think that the debtor should be entitled to apply for a time to pay order (such as we recommend later) relating to those expenses, which would have been taxed and decerned for by the time such an order became competent.

3.20 *Decrees not decerning for principal sum.* We considered whether a time to pay direction should be permitted in those many cases of "non-monetary" decrees in which the only sum of money payable is an award of expenses: examples include decrees of declarator, interdict, ejection or removing, specific implement of a non-monetary obligation, or a "self-executing" decree changing a person's status (e.g. divorce) or making some appointment (e.g. of a judicial factor). We propose, however, that while a person held liable in expenses in such cases should be entitled to apply for a time to pay order such as we recommend later, he should not be entitled to obtain a time to pay direction in the action, petition, application or other proceedings in which the non-monetary decree finding expenses due was granted. In many of those proceedings, the expenses would not have been taxed at the time when the non-monetary decree was granted. It would be more satisfactory to allow the question of an extension of time to pay the expenses to be considered in an application for a time to pay order which would be made at a stage when the expenses had been quantified and where it would be possible for the court to apply the monetary limit recommended later. The practical difference between decrees for payment of a principal sum and other decrees is that in

[1] R.C. 348 (substituted by S.I. 1983/826).

[2] Ordinary Cause Rules, rules 97 and 98. In undefended ordinary cause actions expenses are normally not taxed but modified at a fixed amount and decerned for in the decree for the principal sum.

the former case it would be convenient to allow expenses to be dealt with in the application for a time to pay direction relating to the principal sum, whereas in the latter case there is no principal sum and the same considerations of practical convenience do not arise.

3.21 We **recommend:**

(1) In an action for payment of a principal sum, the court's power to make a time to pay direction relating to the expenses of the action should be exercisable only when it grants decree decerning for payment of the principal sum and either decerning for payment of the expenses or making a finding as to liability for the expenses; and accordingly where the expenses are taxed by the auditor of court at a later stage, a time to pay direction relating to those expenses should not be competent at that stage.

(2) Where the court grants a decree not decerning for payment of a principal sum but making a finding as to liability for expenses (whether or not the decree also decerns for payment of the expenses), it should not be competent for the court to make a time to pay direction relating to those expenses.

(Recommendation 3.5; clause 1(1) and (2).)

Monetary upper limit on debts subject to time to pay directions

3.22 We propose that there should be a monetary ceiling on the debts subject to time to pay directions, which we suggest should be fixed initially at £10,000 of principal sum exclusive of interest and expenses.[1] In the absence of such a ceiling, there would be a risk that applications for time to pay large sums would often be hotly contested and the resulting hearings or proofs would cause unacceptable additional delay and expense. We are primarily concerned in this report with the debts of consumers and small traders. To require the court to consider how and when very large debts should be paid would, in our view, encroach on an area which ought to be dealt with under the general law of sequestration and personal bankruptcy.

3.23 *Interest.* For practical reasons, interest accruing after decree must be excluded from the monetary limit since at the time of decree it would not yet be due, quantifiable or capable of even approximate estimation. For the purpose of the various monetary limits on jurisdiction, interest whenever accrued is generally disregarded and it seems appropriate to disregard interest, whenever accrued, when applying the monetary limit. As recommended above, however, interest should be subject to a time to pay direction to the extent that it is quantified in the decree or claimed by the procedure which we have proposed.

3.24 *Expenses.* We think that the expenses of the action for payment should be excluded from the monetary limit. We concede that the expenses might be a very large amount which could greatly exceed the principal sum. On the other hand, we noted above that in some cases, at the time when decree on the merits of an action is pronounced, the expenses of one party for which

[1]The present jurisdictional limit on summary cause actions for payment is £1,000 (exclusive of interest and expenses): Sheriff Courts (Scotland) Act 1971, s. 35(1)(*a*) as amended.

another party is liable have often not been precisely quantified, since at the time of decree they have yet to be taxed by the auditor of court. In such cases, it would be unsatisfactory to require the court to make an estimate of what the amount of the expenses might be after they have been taxed: those expenses might be impossible to estimate even approximately.

3.25 We **recommend:**

The court's power to make a time to pay direction should be exercisable only if the principal sum (i.e. disregarding interest and expenses) does not exceed a monetary limit fixed by statute at £10,000 initially but variable by statutory instrument.
(Recommendation 3.6; clause 1(4)(*a*) and (6).)

Effect of time to pay decree on diligence

3.26 The object of a time to pay decree is to give a debtor in financial difficulties a breathing space in which to settle his debt, by instalments or deferred lump sum, free from the threat of diligence or further diligence. The question arises of what modes of diligence should be precluded or otherwise affected by time to pay decrees. In answering this question, it is convenient to deal separately with the following categories:

(1) the diligences used for the enforcement of a court decree constituting an ordinary unsecured debt, namely: poinding and warrant sale; earnings arrestment (such as we recommend in Chapter 6); arrestment and action of furthcoming; arrestment and action of sale (of vessels); action of adjudication for debt; and inhibition;

(2) diligences used (a) while the court action in which the decree was pronounced was pending (i.e. arrestment or inhibition on the dependence), or (b) in security of future or contingent debts used before the court action was raised or while it was pending (i.e. arrestment, inhibition, or adjudication in security); and also (c) adjudications for payment of debts subsequently constituted by decree; and

(3) special forms of diligences used for the enforcement of particular categories of debt (i.e. sequestration for rent or feuduty under the landlord's or superior's hypothec; poinding of the ground; action of maills and duties).

We consider these categories in that sequence.

3.27 *Diligences in execution enforcing unsecured debt.* The characteristics of poinding and warrant sale, arrestment and furthcoming and the recommended new diligence of earnings arrestment, are described elsewhere in this report.[1] Though the hybrid diligence of arrestment and sale of a vessel has special features (it resembles a poinding more than an arrestment), it shares with poinding and arrestment of goods the common feature that it is a means of satisfying a debt out of the proceeds of sale of the debtor's property. To allow the debt to be enforced by any of the diligences mentioned in this paragraph while a time to pay decree was in operation would defeat the whole object of the time to pay decree.

[1]Chapters 2, 5 and 6.

3.28 An action of adjudication for debt is the diligence used for the recovery of debt from specific items of heritable property (land or buildings) of a debtor. A decree of adjudication for debt confers on the creditor a right over the adjudged lands in the nature of a heritable security redeemable on payment of the debt.[1] During the legal period of redemption (called "the legal", for short) of 10 years from the decree, the creditor may obtain a decree of maills and duties entitling him to enter into possession and to collect the rents (if any)[2] in satisfaction of his debt. At the expiry of the legal without full payment, the creditor can obtain an indefeasible title as full owner of the adjudged property by obtaining and recording a decree of declarator of expiry of the legal. The main features of this procedure were fixed in the seventeenth century[3] and vividly reflect the desire of a bygone age to preserve landed estates from being involuntarily alienated for debt. Despite its defects, the diligence is still used in a small number of cases annually[4] and we shall propose reforms in due course. In the meantime, the diligence has to be assessed in its present unsatisfactory form. Despite the fact that the diligence takes the form of an attachment coupled with a long period of possession (with or without receipt of rents) followed by ownership, rather than (as in the case of poindings and arrestments) taking the modern form of an attachment followed by the relatively speedy realisation of property to satisfy debts, we think that a time to pay decree should preclude an adjudication for debt while the time to pay direction in the decree is in operation. A time to pay decree would be of little use if the debtor could be ejected from his home by an adjudging creditor. Furthermore, if the adjudged property yielded rents, payment of these rents to the adjudging creditor would be inconsistent with the terms of the time to pay direction.

3.29 Different considerations, however, apply to inhibitions, the remaining diligence available for the enforcement of unsecured debts to be considered. Inhibitions, like adjudications, affect heritable property but are much more commonly used than adjudications.[5] We think that a time to pay decree should not preclude the registration of an inhibition enforcing the debt to which the decree relates. An inhibition is merely a prohibitory diligence whereby, once the inhibition is registered in the personal registers, (a) the debtor's heritable property is rendered "litigious" so that the debtor is restrained from granting any voluntary deed alienating or burdening it to the prejudice of the inhibiting creditor, and (b) the inhibiting creditor is given a preference, in any process of ranking over the debtor's heritable estate, in a competition with other creditors whose debts were created subsequent to the registration of the

[1]Title is completed by recording the extract decree in the Sasines or Land registers in the case of registrable interests in land and in the Register of Inhibitions and Adjudications in the case of non-registrable interests such as leases or other "personal" rights to land. The action is privative to the Court of Session.

[2]If the debt is satisfied from the rents or otherwise, the debtor may obtain a decree of declarator of redemption but payment by itself extinguishes the adjudication without the need for such a declarator.

[3]Diligence Act 1661; Adjudications Act 1672.

[4]We have been informed by the Deputy Principal Clerk of Session that during the six years 1979 to 1984, a total of 40 decrees of adjudication for debt were extracted, an average of almost seven *per annum*.

[5]In 1982, 5,720 inhibition documents (including inhibitions and notices of inhibition) were registered: *Civil Judicial Statistics Scotland,* Table 25.

inhibition. Thus the registration of an inhibition does not create a nexus over specific items of property, nor does it enable the inhibiting creditor to realise the property and to satisfy his debt out of the proceeds. In this respect it differs from poinding and sale and from arrestment and furthcoming or sale. Further an inhibition does not enable the creditor to possess, and to consume the fruits of, the debtor's property (as in the case of adjudications for debt) nor to acquire absolute ownership thereof (as in the case of adjudications for debt on which declarator of expiry of the legal has followed, and those poindings and arrestments in which the attached property is adjudged to belong to the poinding or arresting creditor in default of sale). In short, in contrast to these diligences, an inhibition would generally not be inconsistent with the provisions of a time to pay decree. Moreover, a consumer or small trader in financial difficulties is less likely to be adversely affected by an inhibition than by diligence against his moveable property and funds. In any event, in principle a debtor having the privilege of time to pay should not incur new debts prejudicing the creditor in the time to pay decree, and it therefore seems reasonable that that creditor should be entitled to register an inhibition giving him a preference over debts contracted after the inhibition in any process of ranking on the debtor's heritable property.[1]

3.30 *Diligence on the dependence.* No provision is made by the existing law as to the effect of a summary cause instalment decree on a pre-existing arrestment on the dependence (which is in effect for most purposes converted by the decree into an arrestment in execution[2]) or indeed a pre-existing inhibition on the dependence. (Though competent, the latter are probably very rare for procedural reasons.[3]) The matter will require explicit regulation however if, as we envisage, instalment decrees become available in all actions for payment, in some of which diligence on the dependence is used relatively frequently. Broadly the same considerations apply here as in the case of diligence in execution of decrees. Where an arrestment had been used on the dependence of an action in which a time to pay decree was granted, a furthcoming or a sale of the arrested funds or moveable property would be inconsistent with the terms of the time to pay decree. We think therefore that the court granting a time to pay decree should have power to recall or restrict an arrestment on the dependence and, if the arrestment was not recalled by the court, it should be, so to say, "frozen" so that it could not be followed by an action of furthcoming or sale while the time to pay direction in the

[1]By making arrestments and adjudications incompetent but inhibitions competent, our recommendations could lead to difficulties if the courts were to hold that where the property is sold by a heritable creditor, an inhibiting creditor has no title to claim payment from the free proceeds unless he had adjudged before the sale or arrested after it. This is not, however, the present practice of the courts: see *Halifax Building Society* v. *Smith* 1985 S.L.T. (Sh.Ct.) 25, 30: compare Gretton, "Inhibitions and Standard Securities" 1985 S.L.T. (News) 125.

[2]*Abercrombie* v. *Edgar and Crerar* 1923 S.L.T. 271.

[3]The former rule making inhibitions incompetent on the dependence of a sheriff court small debt action (see *Lamont* (1867) 6 M. 84 construing the Small Debt (Scotland) Act 1837, s. 13) does not appear to apply to summary causes, decrees in which are not enforced by special procedures. Warrant to inhibit on the dependence of sheriff court actions is obtained by an application to the Petition Department of the Court of Session for authority to obtain signeted letters of inhibition. In all other cases, warrant to arrest or inhibit on the dependence of a Court of Session action and to arrest on the dependence of a sheriff court action may be inserted in the summons or initial writ by which the action is commenced.

decree was in force.[1] On the other hand, an inhibition on the dependence should be treated in the same way as an inhibition in execution for the reasons just discussed, and accordingly should continue in force unaffected by the time to pay decree.

3.31 We appreciate that the power to recall or restrict an existing arrestment on the dependence represents a novel encroachment on rights already vested in the creditor and to that extent the position differs from the prohibition of future arrestments in execution. We argue later that the court should have power to recall or restrict arrestments in execution and to recall poindings when making a time to pay order after decree for payment has been granted[2] and the same considerations apply to arrestments used on the dependence. To mitigate so far as practicable the possible adverse consequences to creditors, we advance certain recommendations. First, we think that where the court is minded to recall an arrestment on the dependence, it should have power to impose such conditions as it thinks fit on the debtor which he must satisfy before the court will make a time to pay direction and an ancillary order recalling the arrestment.[3] In such a case, we propose that the court would defer pronouncing decree constituting the debt and continue the case for a period to allow time for the debtor to fulfil the conditions.[4] For example, the court might require the debtor to give the arrestee an irrevocable mandate for payment to the creditor of funds arrested on the dependence as a condition precedent to the grant of a time to pay direction for payment of the balance of the debt by instalments.[5] The court should retain its common law powers to recall or restrict an arrestment (and indeed an inhibition) on caution or consignation and on grounds that the diligence was "nimious" (i.e. excessive) and oppressive or incompetent.

3.32 Second, as an additional safeguard for creditors, we recommend later[6] that the recall of an arrestment on the dependence should not affect the rights which a creditor may have acquired through his arrestment to participate in other diligences which had been equalised with his arrestment by bankruptcy legislation.[7]

3.33 *Diligence in security.* It is competent to arrest and inhibit in security of a debt which is future (i.e. payable on a date certain to arrive but not yet

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[1]It should be noted that under the present law an arrestment of earnings and pensions is not competent on the dependence of an action: Law Reform (Miscellaneous Provisions) (Scotland) Act 1966, s. 1, and under our recommendations the new diligence of earnings arrestment (which requires payment without the need for a furthcoming) would likewise not be competent on the dependence.

[2]See para. 3.89.

[3]The sheriff in a summary cause action has already power to attach conditions to an instalment decree under the Sheriff Courts (Scotland) Act 1971, s. 36(4), but we understand that the power is rarely, if ever, used.

[4]In this way, the same provisions on appeals would apply to the time to pay direction and to recall as to the principal provisions of the decree. The alternative of pronouncing decree constituting the debt and superseding extract pending fulfilment of the conditions would entail separate provisions on appeals.

[5]As the expense of an arrestment on the dependence is not chargeable against the debtor (Graham Stewart, p. 133), payment of those expenses should not be a condition of recall.

[6]See para. 3.102.

[7]Bankruptcy (Scotland) Bill 1984, Sched. 7, para. 10, re-enacting with minor modifications the Bankruptcy (Scotland) Act 1913, s. 10.

come) or contingent (i.e. payable on the happening of an event which may never occur)[1] if there are "special circumstances" justifying the court in granting warrant for such diligence.[2] There are authorities suggesting that warrant for diligence in security will be granted only when the future or contingent debt has been duly constituted by a bill of exchange, bond or decree.[3] However, this category overlaps with diligence on the dependence: indeed, most recent reported cases on diligence in security concern actions concluding for financial provision on divorce or aliment in which the warrant is granted both "in security" and "on the dependence", and where the debt has not yet been constituted.[4] While we have recommended that time to pay decrees should not be competent in respect of financial provision and aliment, these cases are cited here as showing that diligence in security is indeed in some circumstances competent before a debt has been constituted by a bill of exchange, bond or decree. There might be other circumstances as yet not identified in which warrant for diligence in security was granted otherwise than on the dependence of an action and was then followed by an action in which a time to pay decree was granted.[5] If such a case should arise, we propose that the arrestment, but not the inhibition, should be subject to recall or restriction by an order ancillary to the time to pay decree.

3.34 It appears that "adjudication in security may be used when the debt is future or contingent, and the debtor is *'vergens ad inopiam'*" (scil. verging on insolvency), "or when the claim is uncertain in amount".[6] The adjudication is only a security and does not become an irredeemable right after 10 years.[7] Such diligence appears to be unknown in modern practice since creditors can use inhibitions in security of future or contingent debts, and we do not think that, pending our proposed review of adjudications, specific legislation is required in connection with time to pay decrees.

3.35 Summarising the foregoing proposals, we **recommend:**

(1) A time to pay decree, while it is in operation, should render the debt unenforceable by a charge for payment and by the diligences used for enforcing payment of ordinary unsecured debts, namely, poinding and warrant sale, earnings arrestment (recommended below), arrestment and action of furthcoming, arrestment and action of sale (of vessels), and adjudication for debt, but should not prevent the registration of an inhibition based on the debt.

(2) On making a time to pay decree, the court should have a new discretionary power to make an ancillary order recalling or restricting an existing arrestment on the dependence of the action in which the decree was granted, or an existing arrestment in security of the debt

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[1]Graham Stewart, pp. 15 and 528.

[2]E.g. that the debtor was verging on insolvency, or contemplating abscondence or disposing of assets to the possible prejudice of the creditor: see *Wilson* v. *Wilson* 1981 S.L.T. 101.

[3]Graham Stewart, p. 15; *Mitchell* v. *Scott* (1881) 8 R. 875, 879.

[4]See e.g. *Gillanders* v. *Gillanders* 1966 S.C. 54; *Brash* v. *Brash* 1966 S.C. 56; *Tweedie* v. *Tweedie* 1966 S.L.T. (Notes) 89; *Wilson* v. *Wilson* 1981 S.L.T. 101.

[5]An example would be if the creditor in a bill of exchange or bond, instead of using summary diligence, sought for some reason to constitute his debt by court action.

[6]Graham Stewart, pp. 665–6.

[7]*Idem.*

to which the decree relates. This ancillary power should be additional to its common law powers to recall or restrict arrestments on the dependence or in security.

(3) The court should be empowered to impose on the debtor conditions which must be fulfilled before the making of the ancillary order, and to defer pronouncing decree to allow time for the debtor to fulfil the conditions.

(4) The foregoing ancillary power should not apply to inhibitions on the dependence or in security or adjudications in security.
(Recommendation 3.7; clause 2).

3.36 *Adjudications for debt.* It is competent to raise an action of adjudication for payment of a debt (as distinct from adjudication in security) if the debt is quantified in a liquid document of debt (such as a bond, bill of exchange or promissory note), even though the debt has not been constituted by decree, or the document of debt or a protest of the bill of exchange or promissory note has not been registered for execution in the books of court.[1] It is possible, therefore, that an adjudication for payment of a debt could be completed and the debt subsequently constituted by decree in an action for payment. It is necessary to consider what provision should be made for such a case (admittedly rare in modern practice): what should be the effect of a time to pay direction on the pre-existing adjudication, or indeed *vice versa*? Should a time to pay direction be competent while the adjudication subsists? Should the court extinguish the adjudication, or should the adjudication preclude the time to pay direction? What if the adjudication and payment actions were proceeding concurrently? This minor problem might well be solved satisfactorily by reforms made to adjudications,[2] but in the meantime, as an interim solution pending our review of adjudications, we think that any legislation introducing time to pay decrees should restrict actions of adjudication for debt to cases where the debt had already been constituted by decree or decree of registration.[3] This would have the merit of legislative simplicity and would only adversely affect creditors who wished to adjudge and who held a document of debt which was liquid but not registrable for execution.

3.37 We **recommend:**

It should not be competent for a creditor to raise an action of adjudication to enforce a debt payable under a liquid document of debt or a bill of exchange or promissory note unless:

(*a*) the debt has been constituted by a decree; or

(*b*) the document of debt, or a protest of the bill of exchange or the promissory note, as the case may be, has been registered for execution in the books of court.
(Recommendation 3.8; clause 126.)

3.38 *Special modes of diligence.* While a time to pay decree should affect the diligences used to enforce ordinary unsecured debts (other than inhibitions),

[1]Graham Stewart, p. 580.

[2]For example, if a warrant to charge and adjudge were granted in a decree for payment instead of in a separate action for adjudication.

[3]I.e. an extract registered document of debt: see para. 2.11.

we think that such decrees should not affect the special diligences used for the enforcement of particular categories of debt which are accorded special privileges or are available only to secured creditors: these are the diligences of sequestration for rent or feuduty under the landlord's or superior's hypothec; actions of poinding of the ground; and actions of maills and duties. We revert later to the effect of a time to pay decree on the remedies of a creditor other than diligence.[1]

3.39 Sequestration for rent is the diligence by which the landlord (of rural subjects of less than two acres and of urban subjects) enforces his hypothec, a species of right in security for rent[2] over the moveable goods which the tenant grows or produces on the land or brings on to it, including in certain circumstances the goods of third parties. The hypothec is imputed by law into the lease and is not created by agreement. It is an exception to the general rule of Scots law that there can be no security over goods without delivery of the goods to the creditor. The superior's hypothec for feuduty is similar. We propose to review this topic in due course with a view to determining whether the hypothec and the diligence of sequestration should be abolished or reformed. Meantime, the dilgence has to be assessed in the light of the theory that it enforces a real right in security and that sequestration for rent can be commenced without constituting the debt by decree. We think that, until the hypothec is reviewed in the light of consultation, it would be premature to propose that it should be affected by time to pay decrees.[3] Sequestrations for rent are not now frequently used.

3.40 An action of poinding of the ground is the diligence available to the creditor in what is called a *debitum fundi* (literally "a debt of the land"), namely, a feudal superior, a creditor in a ground annual or in a real burden for the payment of money and a creditor in a bond and disposition or assignation in security or in a standard security. The creditor can poind goods not only of the debtor but also of the debtor's tenants and of third parties even after the land has been alienated by the debtor. It is both a diligence and a species of real action designed to give effect to the creditor's security for his debt. The existence of this diligence (which is seldom used) prompts certain questions. For example, if there is a case for conferring rights to create securities over moveables without delivery, it seems doubtful whether it can in modern times be confined to the holders of *debita fundi*. And why should such a right be implied by law rather than created by agreement, or affect the goods of third parties? We propose to consult on the question whether this ancient mode of diligence should be reformed or abolished. Pending our review of the diligence, we propose that time to pay decrees should not affect actions of poinding of the ground. Meantime it may be observed that a poinding of the ground is executed in the same manner as a "personal"

[1]See para. 3.103 below.

[2]The hypothec covers only rent which is due or current but not arrears; it secures each year's rent successively and must be put in force within three months of the term of payment: *Encyclopaedia*, vol. 8, p. 6.

[3]As an interim reform, we recommend later that the exemptions from diligence which we recommend for poindings should apply also to sequestrations for rent or feuduty: Recommendation 5.51(4) (para. 5.244). We revert later to sequestrations for rent of moveables on dwellings subject to protected or statutory tenancies restricted by section 110 of the Rent (Scotland) Act 1984: see para. 3.111.

poinding[1] and would thus attract the safeguards for debtors which we recommend in Chapter 5 for personal poindings.[2]

3.41 An action of maills and duties is traditionally classified as a diligence[3] but is essentially a remedy available to a secured creditor whose security deed contains an assignation of rents. A decree of maills and duties gives the creditor a right to enter into possession and clothes the creditor with the debtor's rights as landlord so that the creditor may recover rents and exercise the landlord's hypothec. The action is the equivalent of the statutory right which a creditor in a standard security may obtain to enter into possession and recover the rents.[4] Since standard securities do not assign the rents, actions of maills and duties by heritable creditors (other than adjudgers) will eventually wither away, but meantime, like other rights of secured creditors,[5] they should not be affected by time to pay decrees.

3.42 We **recommend:**

The diligences to be rendered unenforceable by a time to pay decree or subject to recall by an order ancillary to such a decree, should not include a sequestration for rent or feuduty under the landlord's or superior's hypothec, a poinding of the ground or an action of maills and duties. (Recommendation 3.9; clauses 2 and 11(1)(*a*).)

Intimation of time to pay decree and automatic lapse of time to pay direction on default

3.43 A direction for payment by instalments in a summary cause instalment decree lapses automatically, without the need for any recall by the court of the direction, if the debtor allows one instalment to remain unpaid until the next instalment falls due. Thus in a weekly instalment decree, if the debtor does not pay the first instalment within a week after the due date, he loses altogether his entitlement to pay by instalments. One of the main defects of summary cause instalment decrees is that, in the absence of any legal requirement for intimation to the debtor of the granting of the decree, the debtor may lose the right and opportunity to pay by instalments because he does not get to know about the instalment decree until after the instalment provisions of the decree have already lapsed.[6] In recent years, many sheriff clerks, following advice in circulars by the Scottish Courts Administration, now intimate instalment decrees to debtors but this practice, we understand, is still not adopted in all sheriff courts: it is not required by law.

3.44 We think that the principle of automatic lapse on default is a valuable one and should be retained since it avoids the expense and trouble involved in a creditor's application to the court for recall of the order on default.

[1]There is however no prior charge in a poinding of the ground. A "personal" poinding is a poinding other than a poinding of the ground.

[2]Pending our review of poindings of the ground we have not sought to recommend provisions adapting poinding procedure for poinding of the ground.

[3]See e.g. Graham Stewart, Chapter 25; but cf. *Smith and Others* v. *Bruce* (1916) 1 S.L.T. 29.

[4]Conveyancing and Feudal Reform (Scotland) Act 1970, s. 11 and Sched. 3, standard condition 10(3); s. 24.

[5]See para. 3.118 below.

[6]See e.g. Edinburgh University Debtors Survey, para. 5.8.

Moreover, under a rule of automatic lapse on default, every one knows where they stand. We think, however, that the existing provision should be relaxed in the debtor's favour so that the privilege of time to pay lapses only if the debtor allows an instalment to remain unpaid for two instalment periods (instead of one, as at present): in other words, if the debtor is in arrears with the payment of two (not necessarily consecutive) instalments. On the date when the last instalment falls due, the debtor may be only one previous instalment in arrears or may not be in arrears at all. In such a case, the proposed rule that the direction will lapse only if two instalments remain unpaid when the next falls due would be inappropriate, partly because no further instalment is due on a later date, and partly because there may only be a single instalment remaining unpaid. The debtor should, however, be given a period in which to pay the unpaid instalment or instalments. We propose, therefore, in such a case a simple rule giving the debtor three weeks thereafter to pay the balance of the debt unpaid when the last instalment falls due whatever instalment period is laid down by the direction for previous instalments. Moreover, to cure the defect mentioned in the preceding paragraph, default on payment of any instalment should not be treated as default for the purposes of automatic lapse unless the creditor had already intimated an extract of the time to pay decree to the debtor. We propose that intimation should be made by the creditor rather than the court since creditors will almost always be legally represented and since the creditor will require to know the precise date of intimation in order to ascertain whether the debtor has defaulted and the direction has lapsed. Where a time to pay direction in a decree applies both to sums decerned for in that decree and to sums decerned for in a later decree for expenses, default in payment of sums due under either decree should terminate the privilege of time to pay sums due under both decrees.

3.45 We **recommend:**

(1) Sums due under a time to pay decree decerning for payment of a principal sum should become payable only after intimation by the creditor of the extract decree to the debtor.

(2) Where a court grants a time to pay direction relating to expenses in a decree which either:

(*a*) finds expenses due but does not decern for payment of them; or

(*b*) decerns for payment of the expenses as taxed by the auditor of court but does not specify the expenses as a quantified sum,

the expenses should be payable in terms of the direction only after intimation by the creditor to the debtor of an extract decree for expenses specifying their amount.

(3) The privilege of time to pay by instalments conferred by a time to pay decree should lapse automatically if, on the due date for payment of an instalment, the debtor is already two prior instalments in arrears. If the debtor is in arrears with one prior instalment on the date when the last instalment falls due, or if he is not in arrears but fails to pay that instalment on that date, the privilege should lapse if he had not paid the unpaid balance of the debt within three weeks after that date.

(4) A time to pay direction relating to a deferred lump sum should lapse 24 hours after the time for payment has arrived.

(5) Where the court makes a time to pay direction in a decree for payment of a principal sum and subsequently grants a decree for payment of the expenses of the action, the lapse of the direction through default in paying a sum or sums due under one of the decrees should terminate also the privilege of time to pay the sums due under the other decree. (Recommendation 3.10; clauses 1(1) and (3); and 3(1)–(4).)

Variation and recall of time to pay direction

3.46 At present, a summary cause instalment decree fixes the level of instalments once and for all and the court has no power to vary or recall the instalment provisions of the decree if a material change occurs in the debtor's circumstances. We think that the court should have a power to vary or recall a time to pay direction in a time to pay decree. Such a power might be particularly useful standing the fact that the monetary limit on time to pay decrees would be at a much higher level than under the present summary cause procedure. Thus a debtor should be entitled to apply for a downward variation of the level of instalments if he suffers a loss of income. Further, there is evidence that some debtors offer to pay instalments at a level which they cannot meet[1] and we think that the court should be empowered to vary the instalments if it made the order in ignorance of a material fact even though there has been no material change in the debtor's circumstances. The court should also have a power to recall or restrict an arrestment which had not been recalled when the time to pay decree was made, subject to the debtor fulfilling such conditions precedent (if any) to the recall or restriction as the court might impose.

3.47 Having regard to the serious consequences of default, and to the fact that if a time to pay direction for instalments had lapsed on default the debtor might, under our recommendations,[2] be debarred from obtaining a time to pay order such as we recommend later, we envisage that the form of intimation of an extract time to pay decree should be prescribed by act of sederunt and should notify the debtor of his right to apply for variation of the time to pay direction in the decree. Clearly creditors should also have the right to apply for a variation order or recall order, the grounds of which cannot be foreseen and defined exhaustively in legislation. Variation or recall would often be appropriate if for example the debtor's circumstances improved or it was discovered that he had substantial assets which had not been disclosed when the time to pay decree was made. Recall would or might be appropriate where the debtor granted unfair preferences to other creditors or gratuitous alienations to his family or business associates, to the prejudice of the creditor, or was about to remove assets from the jurisdiction to evade eventual diligence, or irresponsibly incurred new debts, or where a race of diligences by other creditors against his property developed.

3.48 We **recommend:**

[1]See Edinburgh University Debtors Survey, para. 5.6: such offers were made because the debtors felt that smaller payments would not be acceptable to creditors.

[2]See paras. 3.64 to 3.66.

(1) A court which has made a time to pay decree should be empowered to vary or recall the time to pay direction in the decree and, subject to such prior conditions as the court thinks fit, to recall or restrict any arrestment securing the debt, on a subsequent application by the debtor or creditor.

(2) Provision should be made by act of sederunt to ensure that the form of intimation of an extract time to pay decree should notify the debtor of his right to apply for a variation of the time to pay direction in the decree and for recall or restriction of an arrestment securing the debt. (Recommendation 3.11; clause 3(5), (6) and (7).)

Section B. Time to pay orders

Introduction of time to pay orders

3.49 Under the present law, whereas instalment decrees are available at the stage of a summary cause action, it is, as a general rule,[1] not possible for a debtor whose debt has been constituted by an "open" decree for payment to obtain the right to pay by instalments.[2] In our Consultative Memorandum No. 48, we sought views on whether the defender in an action for payment should have the right to apply, after an "open" decree had been granted, for an order substituting an instalment decree for the open decree.[3]

3.50 This suggestion was approved by all who commented and we have no doubt that the reform is needed. We have already noted that whereas a large number of debtors cannot pay outright or can do so only with great difficulty, only a small proportion apply for or obtain instalment decrees.[4] An even smaller proportion of instalment decrees actually operate as such because in some cases default occurs before the debtor even learns that the instalment decree has been granted.[5] If implemented, our recommendation for intimating time to pay instalment decrees[6] would go far towards solving this problem, but we think that the many debtors who do not obtain an instalment decree at the stage of the court action should nevertheless be entitled after decree for payment has been granted to apply for an order converting an open decree into an order (which we call a "time to pay order") similar to a time to pay decree. It would be unduly harsh to deny a debtor such a right on the ground that he should have applied for an instalment order in the court action and has only himself to blame if he did not take that opportunity. Quite apart

[1] As an exception to the general rule, the Moneylenders Act 1927, s. 18(*f*) enabled the court to make an instalment order at any time before payment in relation to sums due under a moneylender's agreement, and a time order under the Consumer Credit Act 1974, s. 129(1)(*b*), is also competent after decree.

[2] Under the present law, in the case of a decree in absence, provision is made for "reponing" debtors (i.e. allowing them to defend the action though decree has been pronounced) at the court's discretion in a sheriff court ordinary action (Ordinary Cause Rules, rules 28–32) or as of right in a sheriff court summary cause action (Summary Cause Rules, rule 19) (cf. R.C. 89(*f*)). But the procedure is designed to allow the debtor to put forward a defence and we understand that, in the case of summary cause actions, it is generally accepted that the reponing procedure cannot be used for the purpose of enabling the sheriff to substitute an instalment decree for an open decree.

[3] Paras. 1.20 to 21, Proposition 1(2) (para. 1.26).

[4] See paras. 2.26 to 2.27 above.

[5] Para. 3.43 above.

[6] Recommendation 3.10(1) and (2) (para. 3.45).

from cases in which the debtor's inability to pay arises only after decree is granted, e.g. through supervening illness or unemployment, very many debtors already pay decree debts by instalments under informal arrangements and one complaint about the present law is that the instalments are fixed by creditors at an unduly high level. Moreover, many debtors do not appreciate their predicament until some enforcement steps have been taken. Such debtors should have the opportunity to obtain a court order fixing the instalments at an appropriate level.

3.51 We note that the county courts in England and Wales possess general powers to stay enforcement proceedings on the ground of inability to pay and to substitute instalment orders.[1] The Payne Report observed that these powers constitute a "satisfactory code"[2] and that there is "at each stage power in the court to protect the debtor against the hardship of execution if he is genuinely unable to pay the debt or any instalments ordered".[3] And in Northern Ireland, after a court action, the Enforcement of Judgments Office can make an instalment order, in lieu of an enforcement order attaching property or income.[4] We think that debtors in Scotland should have a similar right to apply to the court for a time to pay order.

3.52 For the reasons given above, the court should also have power to order payment by a deferred lump sum rather than instalments,[5] and title to apply should be conferred on the categories of individuals entitled to apply for time to pay decrees.[6]

3.53 We **recommend:**

(1) A new jurisdiction should be conferred on the courts to make an order (to be called a time to pay order) whereby a debt which has already been constituted by decree would be payable by instalments or by a deferred lump sum.

(2) Time to pay orders should be available to the same categories of persons and subject to the same limitations as are time to pay directions in terms of Recommendation 3.2 above.[6]

(Recommendation 3.12; clauses 4(1) and (2) and 12.)

Debts subject to time to pay orders

3.54 The right to apply for a time to pay order should be available not only in respect of a decree pronounced in an action or other civil proceedings in a Scottish court but also in respect of a decree of registration on which summary diligence may be executed,[7] a "deemed" decree of registration,[8] a

[1]County Courts Act 1984, ss. 71, 86, 88.
[2]Para. 491.
[3]Para. 495.
[4]The Judgments Enforcement (Northern Ireland) Order 1981, article 30 (S.I. 1981/226).
[5]See paras. 3.3 and 3.4.
[6]See para. 3.9.
[7]See para. 2.11 above for an explanation of "decrees of registration" and summary diligence.
[8]I.e. orders rendered by statute enforceable in like manner as an extract registered decree arbitral bearing a warrant for execution issued by a sheriff court: such as the awards of an industrial tribunal under the Employment Protection (Consolidation) Act 1978, Sched. 9, para. 7(2) (as amended).

non-Scottish decree or decree-arbitral enforceable in Scotland on registration under statute[1] or on the granting of a decree-conform at common law, and authentic instruments and court settlements emanating from E.E.C. Member States and any other non-Scottish instruments which are enforceable by diligence in Scotland.[2] These are simply different ways of constituting a debt and obtaining warrant for diligence.

3.55 It is less self-evident that time to pay orders should be made available to rates and tax defaulters pursued by summary warrant.[3] There is a tendency for such debtors to withhold payment long after they would pay ordinary debts.[4] It is also said that the collectors of rates and taxes do not choose their debtors but that is also true of many other "involuntary" creditors, e.g. where the debt arises out of delict, unjust enrichment, aliment, or the supply by a public utility undertaking of gas or electricity to a person who has not previously defaulted. Some may consider that a time to pay order is inconsistent with the summary nature of the diligence procedure for recovering rates or taxes whereas others may think that the absence of any prior court action or opportunity to obtain a time to pay decree justifies this protection. A time to pay order would not be pronounced by the sheriff in an opposed application unless the debtor was genuinely unable to pay, and on balance we are of opinion that time to pay orders should apply to rates and tax arrears pursued by summary warrants.

3.56 We think that, as a general rule, taxes, fines and penalties due to the Crown which are constituted by decree in civil proceedings should also be subject to time to pay orders. This would be consistent with the general principle in the Crown Proceedings Act 1947[5] which declares that such decrees should be enforceable in the same manner as in actions between subjects and not otherwise. We would, however, recommend the express exclusion of fines or penalties for contempt of a civil court[6] or for breach of an order under section 91 of the Court of Session Act 1868 (orders for restoration of possession of goods or specific performance of statutory duties) and also civil fines or penalties for professional misconduct imposed under any enactment regulating the discipline of a specific profession or occupation, where the fine or penalty is payable to the Exchequer.[7]

3.57 Fines and other debts due under the orders of courts of criminal jurisdiction (e.g. sums due under compensation orders and caution for good behaviour), though enforceable by civil diligence,[8] should not be subject to the time to pay jurisdiction since recovery of the fine or other debt is governed

[1]E.g. Administration of Justice Act 1920, Part II; Foreign Judgments (Reciprocal Enforcement) Act 1933, Part I; Civil Jurisdiction and Judgments Act 1982, ss. 4 and 18; Arbitration Act 1950, ss. 36(1) and 41(3); Arbitration Act 1975, s. 3(1)(*b*).

[2]E.g. Civil Jurisdiction and Judgments Act 1982, s. 13.

[3]For the special characteristics of summary warrants and diligence following thereon, see Chapter 7 below.

[4]See para. 7.19 below.

[5]S. 26(1).

[6]An order by a civil court imposing a sentence for contempt is now treated as a civil decree, subject for example to the civil avenues of appeal: *Cordiner, Petitioner* 1973 S.L.T. 125.

[7]See Solicitors (Scotland) Act 1980, ss. 53 and 55. We recommend below a similar enactment relating to messengers-at-arms and sheriff officers: see para. 8.84, Recommendation 8.12(4)(*c*).

[8]Criminal Procedure (Scotland) Act 1975, s. 411.

by a separate code[1] under which the court may *inter alia* allow payment by instalments.[2] Debts due under decrees awarding financial provision (capital sums and periodical allowance) on divorce[3] and aliment, and similar decrees enforcing public law obligations of maintenance, should be excluded from time to pay orders as in the case of time to pay decrees and for the same reason. Analogous debts under non-Scottish judgments and documents of debt enforceable in Scotland by diligence should also be excluded.

3.58 We **recommend:**

(1) A time to pay order should be competent where (a) the debt has been constituted by a decree or other document of debt bearing a warrant for diligence; or (b) the debt consists of or includes tax or rates arrears for the enforcement of which the sheriff has granted a summary warrant authorising diligence.

(2) Such an order, however, should not be competent where:

(*a*) the debt due under the decree consists of or includes financial provision on divorce, or aliment; or

(*b*) the decree provides for the recovery of the cost of supplementary benefit or is a contribution order as mentioned in Recommendation 3.3(*b*);[4] or

(*c*) the debt is due under a non-Scottish decree, analogous to those mentioned above, which is enforceable in Scotland; or

(*d*) the debt is a civil fine or penalty imposed for contempt of court in civil proceedings, or for breach of an order under section 91 of the Court of Session Act 1868, or for professional misconduct under any enactment; or

(*e*) the debt is a fine or other sum due under an order of a court in criminal proceedings.
(Recommendation 3.13; clause 4(1) and (7).)

Stage in debt recovery process when time to pay orders competent

3.59 As mentioned in Chapter 2, we think that the new time to pay jurisdiction should only be invoked where an action to constitute the debt is before the court or where a stage in the debt recovery process has been reached at which the risk of the creditor instructing diligence has become real and substantial: otherwise the resources of the courts would be wasted in dealing with cases which would not in any event proceed to diligence.

3.60 In our view, therefore, whereas time to pay decrees should be available in court actions, time to pay orders should only be available at the later stage when the creditor has proceeded to the next formal step in debt recovery following upon the grant of decree. In the case of poinding and warrant sale

[1]Criminal Procedure (Scotland) Act 1975, ss. 194 and 395–412; Criminal Justice (Scotland) Act 1980, s. 66.

[2]1975 Act, s. 399(1).

[3]When the Family Law (Scotland) Bill 1984, clause 17 takes effect, financial provision will also be competent on the grant of decree of declarator of nullity of marriage, and the same considerations will apply there as to financial provision on divorce.

[4]See para. 3.13 above.

procedures, this step is the service of a charge to pay. We recommend in Chapter 6 that a charge should be a necessary prelude to the service of an earnings arrestment such as we describe in that Chapter. We propose that the form of charge would be prescribed by act of sederunt and that the new prescribed form, in addition to warning the debtor of the legal consequences of non-payment within the days of charge, would also notify him of his entitlement to apply for a time to pay order.[1] In contrast to earnings arrestments, arrestments of moveable property and funds other than earnings in the hands of the debtor's employer should, as under the present law, continue to be competent without a prior charge since *inter alia* the charge might induce the debtor to move funds to defeat the arrestment whereas it is unlikely to induce the debtor to leave his job. In such cases, the debtor could apply for a time to pay order as soon as the arrestment had been laid. The procedure in the diligence of adjudication for debt takes the form of a court action[2] and an application for a time to pay order should be competent when such an action has been raised.

3.61 We envisage that a summary warrant for the recovery of rates and taxes should not be preceded by a charge and we propose that the right to apply for a time to pay order should arise as soon as the summary warrant was granted. In practice, the grant of such a warrant is, and probably would continue to be, intimated to rates or tax defaulters before diligence was commenced so that even without a charge, the defaulter would often have the opportunity to obtain a time to pay order before diligence was executed.

3.62 It would not be right to allow a diligence to be affected by a time to pay order where the diligence had reached such an advanced stage that the order would require relatively expensive diligence procedures already completed to be undone or that the debtor has had ample opportunity to obtain a time to pay order but has simply failed to do so. There ought to come a stage in a diligence when a creditor can know that he may in safety instruct the completion of the diligence. In our view, therefore, a time to pay order should not be competent where a warrant of sale of poinded goods, or a decree of furthcoming of arrested funds or moveables, or decree of sale of an arrested vessel, had been granted, or in the case of a summary warrant poinding, intimation of removal and sale, or of sale, had been made in accordance with the new procedure which we recommend later. Under our recommendations, it would still be possible after a warrant of sale of poinded goods for the creditor *voluntarily* to make an instalment arrangement with the debtor involving cancellation of the arrangements for sale,[3] but an order *imposing* payment arrangements at such a late stage would be unfair to the creditor. In the case of adjudication for debt, a time to pay order should not be competent if the creditor had obtained a decree of adjudication and either entered into possession of the adjudged property with the debtor's consent or acquiescence or obtained a decree of maills and duties or decree of removing or ejection of the debtor. Because of the archaic nature of the procedure one result of this solution would be that the debtor could not obtain a time to pay order relating to that debt for a period of up to 10 years,

[1]Recommendation 9.6(3) (para. 9.31).
[2]See para. 3.28 above.
[3]Recommendation 5.41 (para. 5.197).

the legal period of redemption of adjudged property. However, if (as we shall propose in due course) adjudications are modernised, it seems possible that "the legal" will be drastically reduced and this objection, such as it is, would then disappear.

3.63 We **recommend:**

(1) A time to pay order should only be competent where a charge to pay or arrestment in common form had been executed, an action of adjudication for debt had been raised, or a summary warrant granted, for recovery of the debt.

(2) A time to pay order should not be competent after a diligence enforcing the debt had proceeded to an advanced stage (viz. warrant of sale of poinded goods; intimation of the date of removal or impending sale of goods poinded under the recommended new summary warrant poinding procedure; decree of furthcoming or sale of arrested property; or entry into possession of adjudged property with the debtor's consent or acquiescence or a decree of maills and duties or of removing or ejection relating to such property) and until the date when the diligence had been completed or for any reason had ceased to have effect, after which date a time to pay order should again become competent. (Recommendation 3.14; clause 4(1) and (4).)

Other conditions of competence

3.64 We think that the monetary ceiling applicable to time to pay decrees[1] should apply also to time to pay orders with minor modifications. Thus, if the amount of the debt outstanding at the time when the application for a time to pay order is made (excluding interest but including the sums quantified in the extract decree—any principal sum or expenses of the action decerned for in the decree—and any sums for which the debtor had become liable subsequently, namely the expenses of a prior charge or other diligence so far as chargeable against the debtor) exceeded £10,000 or such other sum as might be prescribed by regulations, then the sheriff should be bound to refuse to make a time to pay order. To assist the court in applying this condition of competence the amount of the debt outstanding should be specified in the application.

3.65 In fairness to creditors, and to encourage debtors either to observe the terms of time to pay decrees and orders or to apply timeously for their variation, a restriction should be placed on the number of times a debtor may obtain an extension of time to pay. So if a time to pay direction or a time to pay order had already been made for the same debt (whether or not it was still in operation or had lapsed through default or been recalled by the court), it should not be competent for the debtor to obtain a time to pay order. To ensure that the court could apply this condition of competence, we think that it should be provided by an act of sederunt that the debtor should include in his application for a time to pay order a statement that no time to pay direction or time to pay order relating to the debt had been made previously.

3.66 We **recommend:**

[1]See paras. 3.22 to 3.25 above.

(1) A time to pay order should be competent only where:

(*a*) the debt (exclusive of interest but including expenses decerned for as a quantified sum in the extract decree and diligence expenses) does not exceed a prescribed sum (fixed initially at £10,000 variable by statutory instrument); and

(*b*) a time to pay direction or time to pay order relating to the debt has not already been made.

(2) Provision should be made by act of sederunt requiring a debtor applying for a time to pay order to state in his application that no time to pay direction or order relating to the debt has been made.
(Recommendation 3.15; clause 4(3) and (6).)

The forum; local and international jurisdiction

3.67 *Forum.* In our view, jurisdiction (in the sense of adjudicatory competence) to make time to pay orders should be conferred on the sheriff court and not the Court of Session. The great majority of debt decrees emanate from the sheriff court and it seems essential that the sheriff court should have jurisdiction. The jurisdiction is one which is best exercised locally and, being of a summary character in which legal representation would not be required, it seems an inappropriate jurisdiction to confer on the supreme court. It would not apply to corporate bodies and is generally not appropriate for very large debts.

3.68 The best argument in favour of a two-tiered jurisdiction is perhaps that Court of Session decrees for payment should be subject to control by the Court of Session not the sheriff court. However, the sheriff court already supervises poindings on Court of Session decrees and may award sequestrations which have the effect of discharging debts constituted by Court of Session decrees. Moreover, the sheriff court is now responsible for the enforcement of criminal fines of whatever amount imposed by the High Court of Justiciary. The sheriff's jurisdiction in time to pay orders would not in any way imply disrespect towards the decrees of a superior court.

3.69 *International and local jurisdiction.* Since time to pay orders have a double aspect of precluding enforcement by the ordinary modes of diligence and making that preclusion conditional on payment by instalments or a deferred lump sum, it is not easy to characterise such orders for the purposes of the various sets of rules which now govern the assumption of jurisdiction by the Scottish courts. In relation to the European Judgments Convention, which determines jurisdiction between domiciliaries of member states of the European communities, time to pay order applications would be likely to be treated as proceedings concerned with the enforcement of judgments so that the courts of the State in which the judgment has been or is to be enforced would have exclusive jurisdiction irrespective of domicile.[1] On this view, the Scottish courts would have jurisdiction to make a time to pay order affecting diligences within Scotland enforcing a judgment of an E.E.C. Member State registered in Scotland for enforcement, and the jurisdiction of the local sheriff courts would be a matter to be determined by reference to the internal law

[1]European Judgments Convention, Article 16(5).

of the Contracting State, in this instance Scots law.[1] A similar rule applies for the allocation of jurisdiction within the different parts of the United Kingdom, under the Civil Jurisdiction and Judgments Act 1982.[2] The 1982 Act also enacts a similar rule for *inter alia* allocation of jurisdiction between the sheriff courts:[3] thus the court of the place where the judgment has been or is to be enforced has exclusive jurisdiction over these proceedings.

3.70 It will be seen that this criterion, while appropriate for example to the rules relating to applications for recall of a particular diligence executed in one place, or to an application for warrant of sale, is not appropriate in the case of a time to pay order stopping new diligences throughout Scotland, and recalling, restricting or freezing diligences already executed perhaps in several sheriffdoms or sheriff court districts. Obviously, not all of these courts can have exclusive jurisdiction to make a time to pay order. In these circumstances, we think that a different rule or rules should be adopted for the assumption of local jurisdiction within Scotland. Most debt decrees emanate from the sheriff court and for these we suggest a simple rule that the sheriff court which granted decree for the debt should alone have jurisdiction to make a time to pay order affecting the debt. This is a clear rule and in most cases will enable a debtor to go to the court of his domicile, though there will be cases where he has changed his domicile or where jurisdiction in the original action was founded on some jurisdictional ground other than the debtor's domicile. It may be helpful for the court to have regard to the process in the original action, and our proposed jurisdictional rule might facilitate this. We propose a similar rule for summary warrants granted by the sheriff. In other cases, such as Court of Session decrees, extract registered documents of debt, and external judgments enforceable in Scotland, we suggest that the debtor's "domicile" within the meaning of the 1982 Act, section 41, would be appropriate. In cases where the debtor was not domiciled within a sheriff court district in Scotland, jurisdiction should be allocated to the sheriff having jurisdiction over a place of business of the debtor or, if he had no place of business in Scotland, to a place where he had property (including income, such as a source or earnings or an arrestable liability of a third party to account to him) against which diligence might be done. The general effect would be that a debtor would normally be entitled to apply to his local sheriff court for a time to pay order. Moreover, transfer of applications between sheriff courts would be competent under general rules of court.[4]

3.71 We **recommend:**

(1) The sheriff courts should have exclusive jurisdiction to make time to pay orders.

(2) The sheriff court which granted the decree for payment or summary warrant for recovery of a debt should have jurisdiction to make a time to pay order affecting that debt. In all other cases, jurisdiction should be conferred on the sheriff court of the place where the debtor is

[1]See Anton, *Civil Jurisdiction in Scotland* (1984) p. 104 who observes that "the rules in Art. 16 specify merely the Contracting State whose courts have jurisdiction under it. It is left to the Contracting States themselves to specify which of their courts should exercise this jurisdiction".

[2]S. 16, and Sched. 4, Article 16(5).

[3]1982 Act, s. 20 and Sched. 8, para. 4(1)(*d*).

[4]Ordinary Cause Rules, rule 19.

domiciled or, if he is not domiciled in Scotland, a place where he carries on business, or if he has no domicile or place of business in Scotland, a place where he has property (or a source of income) liable to diligence.
(Recommendation 3.16; clause 4(2) and (7) (definition of "sheriff").)

Procedural aspects of applications for time to pay orders

3.72 An application for a time to pay order should attract the measures (discussed elsewhere in this report[1]) designed to facilitate "DIY applications" by unrepresented debtors. In general the legislation should set out the main features of the procedure leaving the details to be prescribed by act of sederunt with the possibility of modification being made from time to time in the light of practical experience. The debtor would complete an application in a prescribed form containing an offer to pay the debt by instalments or a deferred lump sum and lodge it in court. The sheriff clerk would be under a statutory duty to assist the debtor in completing the form if requested to do so. To preserve the sheriff clerk's impartiality, the legislation should make it clear that the form would contain the debtor's proposals for payment, not what the sheriff clerk thought that the debtor could or should pay. The sheriff clerk should, in our view, have immunity from actions for breach of this statutory duty.

3.73 In framing a time to pay order, the court would require to refer to particulars of the extract decree or other document of debt[2] whose provisions the order will qualify. One practical difficulty here is that the extract decree or other document will invariably be in the possession of the creditor not the debtor and, in the absence of special provision, would generally not be known to the sheriff and sheriff clerk dealing with the application. The debtor, however, should normally be able to obtain these particulars, e.g. from the form of charge or the poinding or arrestment schedule or intimation of earnings arrestment which preceded his application or perhaps even from the court granting the decree or from the creditor. An act of sederunt should provide that where possible the debtor should specify these particulars in his application and the form of charge and other diligence documents served on a debtor should warn him that this information will be required if he applies for a time to pay order. Where the debtor was unable to furnish these particulars to the court, the sheriff should have a power to order the creditor to furnish them, on pain of interdict against further diligence, or of recall of existing diligence, enforcing the debt.

3.74 If the application had been properly made and it appeared that the making of a time to pay order would be competent, the sheriff clerk would send a copy to the creditor, who would have 14 days within which to object to the granting of the application. It is envisaged that objections would normally be made by lodging a simple prescribed form. If no objections were made the sheriff would dispose of the application by granting a time to pay order giving binding legal effect to the debtor's proposals for payment. We

[1]See the summary at paras. 2.136 and 2.137 above, and paras. 9.27 to 9.31 below.

[2]Including a summary warrant and relative certificate of arrears by the collector of rates or taxes so far as applicable to the debtor in question.

envisage that an objection would take the form of either an outright objection to the making of any time to pay order or an objection to the terms proposed by the debtor, e.g. as to the amounts of, or intervals between, the instalments proposed. It would be for consideration whether intimation to the debtor of the objection should be made by the sheriff clerk or by the creditor (or his agent). The debtor would have an opportunity to make representations on the creditor's objections. Only if agreement was not reached as to whether a time to pay order should be made or as to its terms would a hearing be held. In this way, it is hoped that the procedure would normally be carried through on paper without the need for court hearings attended by the parties or their representatives.

3.75 The sheriff clerk would intimate the sheriff's decision to the parties. Since, under our recommendations, a time to pay order providing for instalments would only lapse if there were default in payments after the order had been intimated by the sheriff clerk to the debtor, the sheriff clerk would require to inform the creditor that he had intimated the order to the debtor on a particular date.

3.76 We **recommend:**

(1) The procedure should be as outlined at paras 3.72 to 3.75 above.

(2) So far as the procedure in an application for a time to pay order is not prescribed by clauses 5 and 6 of the Bill annexed to this report, it should be prescribed by act of sederunt. Provision should be made by act of sederunt to secure that where possible a debtor applying for a time to pay order should furnish particulars of the decree concerned to the sheriff and those particulars should be set out in the charge and other documents served on a debtor in the execution of diligence. (Recommendation 3.17; clauses 5 and 6.)

Time to pay orders and diligence

3.77 Since time to pay decrees and time to pay orders would share the same social and legal policy aims, it seems clear that they should preclude broadly the same modes of diligence. Accordingly, in line with our recommendations for time to pay decrees, we envisage that a time to pay order would prevent use of the diligences whereby ordinary unsecured debts are enforced, other than inhibitions. A major difference, however, flows from the fact that time to pay orders would be available at the later stage of debt recovery when diligence in execution of a decree had begun. Whereas time to pay decrees would generally not affect existing diligences other than arrestments used on the dependence or in security, time to pay orders would affect all existing poindings, arrestments, earnings arrestments and adjudications enforcing the debt due under the decree.

3.78 We have already recommended that the service of a charge or the commencement of a diligence or the grant of a summary warrant should be a condition of an application for a time to pay order, but that a time to pay order should be incompetent where a poinding, arrestment or adjudication enforcing the debt had proceeded to an advanced stage as defined above.[1] Two

[1]Para. 3.63; Recommendation 3.14(2).

key policy questions remain. First, how far (if at all) should a creditor be entitled to proceed with a diligence while an application for a time to pay order was being considered by the court? Second, where the sheriff decided to make a time to pay order, what effect should that order have on existing diligences already commenced by the creditor as well as new diligences not yet begun? We turn now to the first of these questions.

3.79 *Interim sist of diligence.* If time to pay orders are to achieve their object of delaying diligence pending the debtor's compliance with payment arrangements sanctioned by the court, then the creditor must be prevented from completing diligence or from taking steps (such as obtaining warrant of sale) which, under recommendations made above,[1] would render the making of a time to pay order incompetent. Accordingly, if an application has been properly made and it did not appear that the making of a time to pay order would be incompetent, the sheriff should be under a duty to make an interim order sisting diligence pending disposal of the application. The order would be intimated to the creditor concerned by the sheriff clerk (rather than the debtor).

3.80 Because the characteristics of specific forms of diligence enforcing unsecured debt vary somewhat, the interim order would require to have different effects on different diligences. In the case of those diligences which take the form of an "inchoate" attachment of property requiring to be completed either by a sale (poinding and sale under ordinary decrees or summary warrants, arrestment and furthcoming of moveable property, arrestment and sale of vessels) or by payment (arrestment and furthcoming of funds other than earnings), the creditor should be entitled to impose the attachment by executing the poinding or arrestment. Otherwise the creditor might fail to obtain the right to claim equalisation with other arrestments and poindings under bankruptcy legislation[2] or the debtor might use the time to pay order procedure to gain time to dispose of his funds and moveable goods. The interim sist should, however, prevent further procedure (such as an application for or the grant of warrant of sale in an ordinary poinding not being an order for the sale of perishable goods; intimation of the date fixed for the removal for sale, or the sale, of goods in a summary warrant poinding; the raising of an action of furthcoming or sale of arrested property or funds and the grant of decree in such an action). If the interim order was made while an application for warrant of sale was pending, that application would fall.

3.81 By contrast, an earnings arrestment such as we recommend in Chapter 6 is a completed, rather than an inchoate, diligence requiring the employer to pay arrested earnings to the creditor without a furthcoming. An interim sist should prevent the execution of a new earnings arrestment but should not affect an existing earnings arrestment: to require the employer to stop deductions and payments pending disposal of the application for a time to pay

[1] *Idem.*

[2] Bankruptcy (Scotland) Act 1913, s. 10 re-enacted with minor modifications by the Bankruptcy (Scotland) Bill 1984, Sched. 7 para. 10. The creditor could claim a *pari passu* ranking on another arrestment or poinding on producing his decree but he might never become aware of the diligence if he has not himself executed an arrestment or poinding.

order, and to restart them if the application were refused, would be unsatisfactory. Moreover, a debtor would have at least two weeks (the days of charge) after a charge was served on him within which to pre-empt an earnings arrestment by application for time to pay and normally would only have himself to blame if he did not take that opportunity. If an earnings arrestment were in operation, the interim sist should not prevent a creditor from sharing in the debtor's earnings by applying for a conjoined arrestment order such as we recommend in Chapter 6, and the interim sist should not affect an existing conjoined arrestment order. Since we have recommended that aliment and periodical allowance on divorce should not be subject to a time to pay order,[1] a time to pay order would not affect the new diligence of current maintenance arrestment recommended in Chapter 6.

3.82 An interim sist of diligence should render incompetent the raising of an action of adjudication for debt.[2] Actions of adjudication for debt are so rare that there is little risk that an adjudging creditor would thereby lose his chance of a *pari passu* ranking by being prevented from adjudging within a year and day after a prior (the first effectual) adjudication in terms of the Adjudications Act 1672.[3] Where an action of adjudication for debt had already been raised, the creditor should be entitled to register a notice of litigiosity in the personal registers, to obtain his extract decree and to complete title by recording the extract in the property registers or an abbreviate in the personal registers. But no further steps (such as the raising of an action of maills and duties and entry into possession of the adjudged subjects, or ejecting the debtor, or collecting rents or the raising of an action of declarator of expiry of the legal) should be competent while the application for a time to pay order was pending. If the creditor had already entered into possession of adjudged subjects or obtained a decree of maills and duties or a decree for removing or ejection of the debtor, then a time to pay order would be incompetent,[4] the application should be refused and no interim sist should be granted.

3.83 We envisage that an interim sist would not preclude the execution of inhibitions or the special modes of diligence described above[5] (which would not be affected by time to pay orders) and it would not prevent the creditor from petitioning for the debtor's sequestration under bankruptcy legislation or applying for a debt arrangement scheme such as we recommend in Chapter 4.

3.84 An interim order sisting diligence should take effect when intimated to the creditor and remain in effect till the sheriff's order disposing of the application was intimated to the debtor and creditor. Certain time limits are, and if our recommendations are accepted will be, imposed on the effective

[1]Para. 3.58; Recommendation 3.13(2).

[2]The debtor's remedy would be an action of reduction in the Court of Session. Specific provisions for clearing the registers of ineffectual adjudication documents comparable to those proposed at paras. 4.119 to 4.124 below for debt arrangement schemes appear unnecessary.

[3]If adjudications were to be reformed and (it may be) the legal shortened, it would be for consideration whether an interim sist should have the same effect on adjudications as we recommend it should have on poindings and arrestments.

[4]Paras. 3.62 and 3.63; Recommendation 3.14(2).

[5]See paras. 3.38 to 3.42.

duration of diligences (such as the three-year period for the prescription of arrestments[1] or the limits recommended below on the duration of poindings[2]). For these purposes, the period of the interim sist should not run against the creditor.

3.85 We **recommend:**

(1) The sheriff should make an interim order sisting diligence by the creditor pending disposal of an application for a time to pay order.

(2) The interim order should not stop the execution of new poindings and arrestments. It should however stop poindings and arrestments from proceeding to warrant of sale or decree of furthcoming or, in a summary warrant poinding, intimation of either removal for sale or sale. It should stop new actions of adjudication for debt and, if such an action had been raised, it should stop the creditor from entering into possession of the adjudged property but it should not stop the registration of a notice of litigiosity in connection with the action, nor the obtaining and recording of an abbreviate or decree of adjudication.

(3) The period during which an interim sist of diligence is in force should be disregarded in computing the period during which by law a diligence subsists.

(Recommendation 3.18; clauses 5(3) and 7; Schedule 7, paragraph 2.)

3.86 *Effect of time to pay orders on diligence.* We propose that, as a means of regulating the legal effect of time to pay orders on diligence, the sheriff would have duties or powers to make ancillary orders recalling or restricting diligences or "freezing" them while the time to pay order was in operation. Again different provisions would have to be made for different modes of diligence because of the need to tailor those orders to suit the individual characteristics of each mode.

3.87 First, the new modes of continuous diligence against earnings enforcing "ordinary debts",[3] namely earnings arrestments and conjoined arrestment orders so far as enforcing ordinary debts, could not remain in effect while an instalment time to pay order was in operation because the level of deductions under these diligences[4] would often necessarily be different from the level of instalment payments under the decree, and because the times of deductions under these diligences[5] would often not coincide with the times of payment of instalments under the time to pay order. Moreover, a continuous diligence against earnings would be inappropriate where a time to pay order provided for a deferred lump sum. Accordingly the sheriff should have a duty (not merely a power) to recall any existing earnings arrestment and, if the debt was being enforced by a conjoined arrestment order, to exclude that debt

[1]Debtors (Scotland) Act 1838, s. 22, which we recommend later should not apply to diligence against earnings.

[2]See Recommendation 5.27 (para. 5.130).

[3]I.e. debts other than current maintenance: see Chapter 6.

[4]Which would be determined by applying a statutory sliding scale to the earnings payable on each pay day.

[5]Deductions would be made on pay days and these might, or might not, be at regular intervals, and might be altered subsequent to the time to pay order.

from that order, or to recall that order if the debt was the only one still being enforced by the order.[1]

3.88 In the case of the "inchoate" diligences of poindings and of arrestments in common form, we propose that the sheriff should possess a discretionary power to make ancillary orders recalling the poinding or recalling or restricting the arrestment, but if he did not recall the poinding or the arrestment as the case may be, he should be under a duty to make an order to the effect that no further steps (such as the making of an application for warrant of sale or the raising of an action of furthcoming or sale) should be taken in the diligence while the time to pay order was in operation. The last-mentioned type of ancillary order would "freeze" the diligence but preserve its effect as an attachment of, or nexus on, the funds or property.[2]

3.89 An ancillary order recalling a poinding or arrestment would be an important abridgement of the vested rights of diligence creditors and we carefully considered whether the lesser power to "freeze" the diligence would suffice or whether the power of recall should be restricted to (say) poindings of goods in debtors' residences and diligence against earnings, which are the main areas of public concern. Such limitations, however, would appear unduly arbitrary and would exclude other deserving cases. For example, it may be that if arrested trading debts or poinded or arrested stock-in-trade or an arrested fishing vessel, were made available to the debtor by a recall of an arrestment or poinding, the debtor could quickly use the released funds or goods to earn the sums needed to pay off the debt. Again, it might be that funds arrested in a bank account were personal earnings of small amount urgently needed for the maintenance of the debtor and his dependants. On balance, we have concluded that the power of recall should in principle apply to all arrestments and poindings.

3.90 As in the case of ancillary orders recalling arrestments on the dependence in connection with time to pay decrees, the sheriff should have power to impose on the debtor conditions precedent to the making of an ancillary order recalling or restricting diligence, and a creditor's right to claim a share in equalised poindings or arrestments would not be affected by the recall of the diligence.[3] We assume that in most cases the sheriff would impose a condition requiring the debtor to pay the expenses of the diligence before recalling it. Where such a condition was not imposed, those expenses should still be recoverable by the creditor from the debtor as an exception to the general rule proposed below[4] that the expenses of a diligence should only be recoverable from the proceeds of that diligence or from payments made before it ceased to have effect. The expenses would also be an element in the debt recoverable by the time to pay order.[5]

3.91 We propose that, on granting a time to pay order, the sheriff should

[1]If the conjoined arrestment order had been made in another sheriff court, a sheriff of that court would exclude the debt or recall the order.

[2]For this reason we have avoided the use of the word "sist" lest it be thought that the order would affect the attachment or nexus on the property or funds imposed by the diligence.

[3]See para. 3.101.

[4]Chapter 9.

[5]See the draft Bill annexed to this report, clause 4(7), definition of "debt".

not have power to extinguish an adjudication for debt, nor if the action of adjudication were pending, to prevent a creditor from registering a notice of litigiosity and obtaining and recording an extract decree or abbreviate of adjudication. However, as in the case of an interim sist,[1] the creditor would not be entitled to take any further steps in pursuing his diligence while the time to pay order was in force.

3.92 Clearly, if a time to pay order was made during the days of charge, the charge should lapse on the making of the order since it requires the debtor to make payment of the debt in full within the days of charge. In the more usual case where a charge had been served and the days of charge had expired before the time to pay order was made, then, unless it can be shown that the debtor was able to pay his debts, his "apparent insolvency" (in the new statutory sense of the term which replaces the concept of "notour bankruptcy" and has similar, though not identical, pre-conditions and effects) would already have been constituted by reason of the expiry of the charge without payment[2] and the time to pay order and its ancillary orders affecting diligence should not retroactively change the legal effect which the expired charge has in constituting the debtor's "apparent insolvency"[3] except that, as we propose below,[4] the debt would not found a petition for the debtor's sequestration for so long as the time to pay order was in operation.

3.93 We **recommend:**

(1) A time to pay order should preclude enforcement of the debt by any new charge, poinding (other than a poinding of the ground), earnings arrestment, arrestment in common form, or action of adjudication for debt.

(2) The sheriff should have:

(*a*) a duty to recall an existing earnings arrestment; to recall, or exclude the debt from, a conjoined arrestment order; and to prohibit further steps in an adjudication for debt other than the registration of a notice of litigiosity and the obtaining and recording of an abbreviate and decree of adjudication; and

(*b*) a power to recall or restrict an arrestment and to recall a poinding (other than a poinding of the ground), and if he does not recall the poinding or arrestment, he should make an order "freezing" the diligence by prohibiting the creditor from taking further steps in the diligence and rendering incompetent the grant of warrant of

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[1]See para. 3.82 above.

[2]Bankruptcy (Scotland) Bill 1984, clause 7(1).

[3]The main effects of "apparent insolvency" are that (1) it makes the debtor liable to sequestration: Bankruptcy (Scotland) Bill 1984, clause 5(2)(*b*); (2) it equalises arrestments and poindings, Bankruptcy (Scotland) Bill 1984, Sched. 7, para. 10; and (3) in the construction of contracts, it replaces "notour bankruptcy" which was and is frequently a condition of an irritancy or other clause in a contract terminating or changing the rights of parties under the contract: 1984 Bill, clause 69(6). With the repeal (by the 1984 Bill, Sched. 8) of the Bankruptcy Act 1696, apparent insolvency or notour bankruptcy is not of itself a pre-condition of the reduction of unfair preferences under statute, and, apart from common law challenges (which were not dependent on notour bankruptcy), unfair preferences are now challengeable if made within six months before sequestration or the granting of a "protected" trust deed for creditors (rather than six months before notour bankruptcy): 1984 Bill, clause 35.

[4]See para. 3.100.

sale or of decree of furthcoming or sale. This freezing order would not however prevent an officer of court from lodging a report of the poinding nor prevent an application for the disposal of perishable goods or for security of goods.

(3) The period during which a diligence is "frozen" by such an order should be ignored in reckoning the time limits on the duration of the diligence.

(4) A time to pay order and its ancillary orders should cause an unexpired charge to lapse but should not retrospectively annul the effect which an expired charge has had in creating "apparent insolvency" within the meaning of bankruptcy legislation.

(5) If the sheriff, being unaware of the existence of a diligence, omits to make an ancillary order recalling, restricting or freezing it as recommended above, the diligence should continue in operation, and further steps may be taken in it, unless and until it is recalled, restricted or "frozen" by a subsequent order.
(Recommendation 3.19; clause 8; Schedule 7, paragraph 2.)

Lapse, variation and recall of time to pay orders

3.94 We propose that the provisions on the automatic lapse of time to pay orders, the variation and recall of such orders, and the recall or restriction (subject to conditions) of unrecalled diligences (poindings or arrestments), securing the debt would closely resemble the corresponding provisions on time to pay decrees.[1] Some special provisions may be noted.

3.95 A sheriff may not have been informed about the existence of a diligence at the time when he made a time to pay order with the result that he did not recall a diligence (e.g. an earnings arrestment) which, under our proposals, he had a duty to recall. Or it may be that he would not have made the time to pay order if he had known of the diligence. In these circumstances, we think that the sheriff should have a power to recall the time to pay order, or to make any order recalling, restricting or "freezing" the diligence which he could have made when granting the time to pay order. The sheriff should be entitled to exercise this power of his own accord after allowing the parties an opportunity to be heard.

3.96 Moreover, we think that, where a poinding was recalled under a time to pay order which subsequently lapses so that the right to do diligence revives, then the creditor should be entitled to execute a second poinding in the same premises for the same debt notwithstanding the restriction on such poindings which we recommend later.[2] The creditor should also be entitled to recover the expenses of the recalled diligence by a subsequent diligence notwithstanding the general rule recommended below that the expenses of a diligence should only be recoverable by that diligence or by payments made before it terminated.[3]

3.97 We **recommend:**

The provisions on automatic lapse of time to pay orders, the variation and

[1]See paras. 3.43 to 3.48 above.
[2]See para. 5.134.
[3]See Recommendation 9.9(5) (para. 9.58).

recall of such orders, and the recall and restriction of existing diligences securing the debt should be similar to the corresponding provisions applying to time to pay decrees, but with minor modifications.
(Recommendation 3.20; clause 9.)

Section C. Recommendations applying to both time to pay decrees and time to pay orders

Sequestration and insolvency

3.98 Under the Bankruptcy (Scotland) Act 1913, a petition for sequestration could be at the instance, or with the concurrence, of any one or more creditors whose debt or debts together amounted to not less than a prescribed sum, whether such debt or debts were liquid or illiquid, provided they were not contingent.[1] Under that Act debts which were payable on a future date certain to arrive would found a petition for sequestration.[2] Under the Bankruptcy (Scotland) Bill 1984, however, such future debts, as well as contingent debts, will not found such a petition. Despite this change in the law, there might be doubt whether a debt to which a time to pay direction or order relates is "future" in the relevant sense. On the one hand, we have proposed that such a debt should be payable on a future date or dates with the effect that it could not be enforced by the ordinary modes of diligence while the direction or order was in operation. On the other hand, the debt, for other purposes such as set off and the enforcement of rights in security, would be treated as presently due and resting owing.[3] In these circumstances, we think that the legislation following on this report should make it clear that a debt to which a time to pay direction or time to pay order relates should not give the creditor the right to present, or to concur in, a petition for the debtor's sequestration while the direction or order is in force. We think that a creditor in a time to pay direction or order who seeks sequestration should first apply to the court for recall of the time to pay direction or order.

3.99 Where the debtor was nevertheless sequestrated by another creditor, it would be unfair to the creditor in the time to pay direction or time to pay order if the direction or order were to continue in effect after the date of sequestration with the possible effect of requiring that creditor to rank as if his debt were not yet due,[4] or to apply for recall of the time to pay direction or order. It should therefore be made clear by statute that the debtor's sequestration terminates a time to pay direction in a decree or a time to pay order. Where the debtor had granted a trust deed for creditors, or had entered into an extra-judicial composition contract with his creditors, or had applied for a debt arrangement scheme such as we recommend in Chapter 4 and a notice had been circulated to creditors requesting them to verify their debts, the debtor would be insolvent and it is likely that other creditors would be enforcing, or threatening to enforce, diligence against the debtor. In these circumstances, the creditor in a time to pay direction or order should be

[1] 1913 Act, s. 12 as amended by the Insolvency Act 1976, Sched. 1.
[2] Goudy, p. 121; Bankruptcy Report, para. 5.31.
[3] See Recommendation 3.24 (para. 3.118).
[4] See Bankruptcy (Scotland) Bill 1984, Sched. 1, para. 1(2) replacing a provision in the Bankruptcy (Scotland) Act 1913, s. 48 as recommended by our Bankruptcy Report, para. 16.12: under both of these enactments, a creditor in a future debt is only entitled to vote and rank after deduction of interest from the date of sequestration until the due date of payment.

placed on a footing of equality with the other creditors by termination of the time to pay direction or order without the need to apply to the court to recall it.

3.100 We **recommend:**

(1) A debt to which a time to pay direction or time to pay order relates should not entitle the creditor to present, or concur in, a petition for the debtor's sequestration while the direction or order is in effect.

(2) A time to pay direction in a decree or a time to pay order should be terminated by an award of sequestration of the debtor's estate, a trust deed for his creditors, an extra-judicial composition contract with his creditors or the circulation of a notice requesting creditors to verify their debts in an application for a debt arrangement scheme such as we recommend in Chapter 4.
(Recommendation 3.21; clause 10.)

Rights acquired under legislation on equalisation of poindings and arrestments

3.101 We have recommended above that the court should have power to recall an arrestment on the dependence of an action in which a time to pay decree was granted or in security of the debt to which the action relates, and also power to recall an arrestment or poinding securing a debt subject to a time to pay order. These powers are designed to benefit the debtor and not to affect the rights of his creditors among themselves. It should be expressly provided therefore that the recall of an arrestment or poinding by an ancillary order in a time to pay decree or order, or any order made on an application to vary the decree or order, should not affect any right which the creditor may have acquired, by virtue of the arrestment or poinding, to share in the proceeds of other arrestments or poindings under bankruptcy legislation[1] which provides *inter alia* that arrestments and poindings executed within 60 days before and 4 months after the debtor's "apparent insolvency" rank *pari passu*[2] as if they all had been executed on the same date. In addition to equalising diligences, the bankruptcy legislation also contains a provision enabling a creditor to claim a share in the proceeds of arrestments and poindings used within the above-mentioned statutory period by producing, in judicial proceedings, a decree for payment or other liquid document of debt. In the absence of a saving clause such as we recommend, a creditor whose arrestment or poinding had been recalled after the expiry of the statutory period might not be able to rely on that provision since his claim might be time-barred. That provision would, however, ensure that if the debtor's apparent insolvency was constituted anew, (e.g. by the expiry without payment of a charge by another creditor), then the creditor in the time to pay decree or order could

[1]Bankruptcy (Scotland) Bill 1984, Sched. 7, para. 10 re-enacting with minor modifications the Bankruptcy (Scotland) Act 1913, s. 10. For the meaning of "apparent insolvency", see para. 3.92 above.

[2]"Pari passu" ranking on a fund involves the sharing of the fund among the creditors rateably according to the size of their debts: i.e. each creditor receives the same proportion of his debt.

participate in the proceeds of later arrestments and poindings by producing his decree within the new statutory period.[1]

3.102 We **recommend:**

The recall of an arrestment or poinding should not affect any right which the creditor had acquired through his arrestment or poinding to a *pro rata* share in the proceeds of other arrestments and poindings under bankruptcy legislation.
(Recommendation 3.22; clause 11(2).)

Preservation of creditors' rights and remedies other than rights to do diligence enforcing unsecured debts and to sequestrate

3.103 *General.* In many cases, the creditor has methods of enforcing his debt other than the ordinary modes of diligence, e.g. security rights; and rights of recourse against cautioners (guarantors). He may also have certain remedies which, though not given by law expressly for the purpose of enforcing debts, can be used for that purpose: notable examples include rights to repossess moveables under a hire purchase, conditional sale or hire agreement; the right of a landlord to remove a tenant for non-payment of rent; or the rights of the public utilities supplying gas or electricity to disconnect the supply for non-payment of gas and electricity charges. Although in theory the use of these special remedies might be regarded as inconsistent with a time to pay decree or order, we think that such decrees and orders must be allowed to apply to debts enforceable by these special remedies. The fact that such creditors have other and perhaps better means of enforcing their debts than the ordinary forms of diligence should not give them the further advantage of immunity from time to pay decrees and orders precluding use of the ordinary forms of diligence.

3.104 On the other hand, we consider that the right of time to pay conferred on a debtor by a time to pay decree or order should be regarded as in the nature of a privilege or, to use the language of the old small debt procedure, an "indulgence". Whereas such a decree or order should preclude the execution of the ordinary forms of diligence (other than inhibitions) used for the enforcement of unsecured debts, and petitions for sequestration, while the time to pay direction or order is in force, the debt should not be regarded for all purposes as a future debt. So, a time to pay decree or order should not affect the other rights and remedies of the creditor for the recovery of the debt such as rights of set off, retention or lien; rights of recourse against cautioners or co-obligants of the debtor (who themselves would be entitled to apply for a time to pay decree or order if they were individuals); or the exercise of security rights over heritable or moveable property of the debtor, or of a cautioner, securing the debtor's personal obligation of payment, such as rights to call up the security on default or to realise or take possession of the secured property to satisfy the debt.

[1]The Bankruptcy (Scotland) Act 1913, s. 7 (reversing *Wood* v. *Cranston and Elliot* (1891) 18 R. 382) provided that a second or subsequent constitution of notour bankruptcy was available for the purpose of the equalisation of diligences, etc. under the 1913 Act, s. 10 and we understand that amendments will be moved to the Bankruptcy (Scotland) Bill 1984, designed to ensure that "apparent insolvency" may be constituted anew for the purposes of the equalisation of diligences under para. 10 of Sched. 7 to that Bill.

3.105 Two categories of debts enforceable by these additional methods of recovery merit fuller consideration here, namely rent arrears, and gas and electricity charges. (At the end of this Chapter, we deal with a third category—consumer credit agreements—to which rather different considerations apply.)

3.106 *Public sector tenancy rent arrears.* Any new system of time to pay decrees and orders must take account of the fact that public sector tenancy rent arrears are normally enforced by actions for recovery of possession followed by the threat of ejection rather than by actions for payment followed by the threat of poinding and arrestment, though some housing authority landlords, at least in the recent past, obtain or have obtained combined decrees for possession and payment, or for payment only.[1] The use of possession actions to recover rent arrears was in effect sanctioned by the Tenants' Rights Etc. (Scotland) Act 1980, Part II which gives the sheriff, in possessory actions by public sector landlords, a new statutory power to adjourn the proceedings for a period or periods "with or without imposing conditions as to payment of outstanding rent or other conditions".[2] Moreover, the sheriff can refuse decree not only if the landlord fails to establish non-payment of rent but also if it appears to him that it is not "reasonable to make the order".[3]

3.107 The courts grant adjournments only where the tenant or his representative comes to court and applies for an adjournment. Recent research[4] has disclosed that in many court districts, tenants or their representatives have been slow to do this and indeed of the sample of 10 sheriff courts studied, in only two (Edinburgh and Glasgow sheriff courts) were applications for adjournment made in significant numbers. Broadly speaking, the Act appears to be operated as follows. If the tenant makes an offer of weekly payments towards the arrears, the action will be adjourned for six to eight weeks to test his ability to keep to the arrangement. If at the end of that period, the tenant has indeed complied with the arrangement, the case will be sisted so that the arrangement can continue without the necessity of calling the case in court at regular intervals. If the tenant has not kept to the arrangement at the end of the period of adjournment but has some reasonable excuse for his failure (e.g. absence from work through illness), he may be allowed a further adjournment prior to the case being sisted. Where a case is sisted but the arrangement breaks down with no apparent likelihood of resumption, the landlord authority will apply to have the sist recalled and will move for decree.

3.108 Once the possessory decree is granted, the position of the tenant in strict law is the same as it was before the 1980 Act: the delaying power of the court under the 1980 Act is exercised before, and not after, decree. As regards

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[1]The O.P.C.S. Defenders Survey, p. 17, discloses that, in a representative sample interviewed in 1978, 63% of local authority actions were actions for recovery of possession without a crave for payment.

[2]1980 Act, s. 15(1).

[3]*Ibid.*, s. 15(2).

[4]Adler, Himsworth and Kerr, *Public Housing, Rent Arrears and the Sheriff Court* (1985) Scottish Office Central Research Unit Papers.

enforcement of the decree by ejection a recent Scottish Office Central Research Unit study observed:[1]

> "Given that most eviction procedures resulted in a payment arrangement, it seems more logical for authorities generally to pursue either joint actions,[2] or, where comprehensive responsibilities under the Housing (Homeless Persons) Act are accepted, actions for payment alone. Nevertheless there are disadvantages—the sum involved can bear no relation to the tenant's final arrears, given delays in court proceedings; the tenant's situation—unemployment or intermittent employment—may limit the suitability of arrestment procedures; while poinding and warrant sales are regarded by most authorities as undesirable and are seldom carried out."

The study recommended:[3]

> "Despite practical problems, authorities might consider whether their arrears can be controlled effectively by recourse to legal action for payment as an alternative or supplement to eviction procedures."

3.109 Under our proposals, the jurisdiction under Part II of the 1980 Act would co-exist with the new jurisdiction to make time to pay decrees and orders. Where the landlord authority brought a combined action for recovery of possession and for payment, the court could exercise its powers under the 1980 Act before granting decree and, in the light of that, would decide whether to grant a time to pay direction at the stage of pronouncing decree in the payment action. Clearly it would be difficult to combine the 1980 Act jurisdiction with the jurisdiction to make time to pay orders in one process since the former is exercisable before decree in a possessory action whereas the latter is exercisable after decree in a payment action. While ejection procedures might sometimes make it impossible for the debtor to comply with a time to pay decree or order, we think that the two jurisdictions can co-exist in a workable fashion and that the new jurisdiction in time to pay decrees and orders would complement the protection afforded to public sector tenants by the 1980 Act.

3.110 *Other rent arrears.* In our view, a similar solution should apply in relation to other types of tenancy, (e.g. private sector tenancies of dwellings; agricultural holdings, crofts and smallholdings): that is to say, rent arrears would be subject to time to pay decrees or orders which would affect the use of ordinary diligences to enforce those arrears but would not affect proceedings for recovery of possession of the subjects of the lease.

3.111 *Rent Act tenancies.* In the case of private sector dwellinghouses let on a protected tenancy or subject to a statutory tenancy under the Rent (Scotland) Act 1984, section 110 of that Act (re-enacting earlier legislation[4]) provides that no diligence shall be done without the leave of the sheriff. In an application for leave to do diligence for the recovery or in security of rent, the sheriff has

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[1]Wilkinson, *Rent Arrears in Public Authority Housing in Scotland* (1980) H.M.S.O. Edinburgh, para. 8.17.

[2]Scil. combined possessory and payment actions.

[3]Para. 8.17.

[4]Rent (Scotland) Act 1971, s. 129(1) which in turn re-enacted, so far as applicable to Scotland, the Increase of Rent and Mortgage Interest (Restrictions) Act 1920, s. 6.

the same wide powers of adjourning proceedings, sist and suspension of execution, as he possesses under the Act in proceedings for recovery of possession of the dwellinghouse.[1] So far as we are aware, applications for leave to enforce rent by diligence are rare. The section derives from a provision in a United Kingdom statute of 1920[2] restricting distress for rent in England and Wales (where a landlord could levy distress without a prior application to the court) with a Scottish application clause substituting "diligence" for "distress".[3] The section does not fit Scottish procedure well: for example, it is not clear whether the application for leave to do diligence should be made in an action for payment and leave granted in the decree authorising diligence, or whether it should be made after decree containing warrant for diligence has been granted but before diligence is commenced or whether the creditor can choose one or other of these alternatives. Moreover, its implications for arrestment on the dependence are obscure. Nor is it clear at what stage in an action of sequestration for rent the application must be made.

3.112 We propose that section 110 of the 1984 Act should be amended in the following ways. First, the restriction imposed by the section should be confined to actions of sequestration for payment of rent, or in security of rent, under the landlord's hypothec. Insofar as the section restricts the ordinary diligences enforcing unsecured debts, we think that it should be replaced by time to pay decrees and time to pay orders partly because these would give just as much protection to a tenant and partly because the co-existence of two different and overlapping protective regimes would be complex and unnecessary.

3.113 Second, since the landlord has to raise a court action of sequestration for rent before he executes the diligence of sale of the sequestrated goods, separate provision for leave to do the diligence is unnecessary and inappropriate. Instead, the sheriff should have a simple discretionary power to adjourn or sist an action of sequestration for rent to enable the debt to be paid. As already mentioned,[4] we propose to review the diligence of sequestration for rent in due course and meantime we think that any amendment of section 110 of the 1984 Act, so far as applicable to sequestration for rent, should make minimal changes. Under the existing law, the sheriff, in his first deliverance in an action of sequestration for rent, makes an order sequestrating the effects and grants warrant to inventory and secure them.[5] At a later stage, the sheriff, on an application by the landlord, grants warrant for sale of the sequestrated effects at the sight of an officer of court or other named person.[6] While we have not found any authority on the Rent Act restrictions, there are sheriff court cases[7] on the analogous restrictions imposed by the Courts (Emergency Powers) Act 1914 in which it was held that leave to enforce under that Act need not be sought before raising an action of sequestration

[1]1984 Act, s. 12.
[2]Cited above.
[3]1920 Act, s. 18.
[4]See para. 3.39.
[5]Ordinary Cause Rules, rule 100; Summary Cause Rules, Form D.
[6]Ordinary Cause Rules, rule 101; Summary Cause Rules, rule 74.
[7]*Jamieson* v. *Portobello Picture Palace Ltd.* (1916) 32 Sh.Ct.Reps. 263; *Marquis of Breadalbane* v. *Toberonochy Slate Quarry Co. Ltd.* (1917) 33 Sh.Ct.Reps. 154.

for rent or before executing the warrant to inventory or secure, or even before decree of sequestration containing warrant of sale was granted. The reason was that a process of sequestration for rent merely identifies and secures the moveable goods subject to the hypothec so as to enable the landlord subsequently to realise his security: diligence within the meaning of the Act was not done until the warrant of sale in the decree of sequestration for rent was executed. We accept this general approach but propose some minor modifications to it. We consider that the tenant should be entitled to apply for a sist or adjournment of the action at any stage from immediately after the time when the first deliverance sequestrating the tenant's effects has been granted to immediately before the grant of warrant of sale of the sequestrated effects. We do not think an application for a sist or adjournment should be competent before the first deliverance. That deliverance is granted before the initial writ has been served on the tenant.[1] To give the tenant an opportunity to oppose the grant of the first deliverance would invite the tenant to remove goods from the dwellinghouse and might greatly diminish the landlord's security. On the other hand, we do not think that a sist or adjournment should be competent after warrant of sale of the sequestrated effects has been granted. Once the proceedings have reached that late stage, the tenant would have had ample opportunity to apply to the sheriff for a sist or adjournment of the action, and the landlord should be able to make arrangements for sale safe in the knowledge that those arrangements will not be disrupted by the court. This solution would give a tenant almost the same protection as under the existing law while achieving a more equitable balance between the interests of the tenant and landlord.

3.114 We **recommend:**

The restriction on diligence enforcing rent imposed by the Rent (Scotland) Act 1984, section 110, should be limited to actions of sequestration for payment, or in security, of rent and should be amended to provide that the sheriff has powers to sist or adjourn the action to enable the rent to be paid by instalments or otherwise which are exercisable at any stage between the first deliverance and the grant of warrant of sale of the sequestrated goods and effects.
(Recommendation 3.23; Bill, Schedule 7, paragraph 34.)

3.115 *Fuel debts.* Unpaid charges for gas and electricity are recoverable as ordinary civil debts.[2] The rights of the fuel authorities to enforce these debts by court action and diligence are extensively used,[3] and these rights are, of course, supplemented by the powers of the fuel authorities to discontinue supplies in the event of non-payment of charges. In the case of default in payment of a charge for electricity, the Electricity Board may cut off the supply until the payment of the sums due together with the expenses of

[1]Dobie, *Sheriff Court Practice*, p. 423.
[2]Gaswork Clauses Act 1871, s. 40 as read with Electric Lighting Act 1882, s. 12; Gas Act 1972, Sched. 4, para. 13.
[3]C.R.U. Court Survey, Table 3A showed that, in 1978, 21% of summary cause payment actions were raised by the fuel boards. The C.R.U. Diligence Survey, Annex D, Table 10, showed that, in the same year, the fuel boards accounted for 15% of debt-related decrees (viz. for payment, possession of heritable property, or delivery of goods) which were enforced.

cutting off the supply.[1] In the case of gas, if within 28 days of a written demand the consumer has not made payment of the charges for the supply of gas, the Gas Corporation may, after seven days' notice, cut off the supply and recover the expense: the Corporation has no duty to restore the supply until payment of all sums due and the expenses of reconnection.[2] These powers were considered by the National Consumer Council,[3] and also by an unpublished report to the Secretary of State for Energy by Mr Gordon Oakes in 1976[4] on payment and collection methods for gas and electricity bills.

3.116 Following these reports and as a result of them, the disconnection powers of the fuel boards are now exercised in accordance with a code of practice in which the fuel authorities state among other things that they will not cut off supply if the defaulting customer agrees and keeps to a payment arrangement for his electricity or gas and pays off the debt by instalments in a reasonable period, or if there is real hardship and it is safe and practical to instal a slot meter.[5] The practice of disconnections and the operation of the Codes of Practice have been much discussed.[6]

3.117 Against this background, three points may be made. First, the question whether judicial or other restraints should be imposed on the powers and rights of the fuel boards to disconnect supplies is strictly speaking not one which falls within the reform of the law of enforcement of debts by diligence. It is nevertheless of considerable importance to debt enforcement. Since the fuel boards may and do use the threat of disconnection to compel or induce payment of arrears—a threat made more potent by their monopoly position and by the essential nature of the energy supplied for the standard of living of the consumer and his family—a case can be argued for introducing restraints on disconnection similar to the restraints on diligence which we are recommending. But the position of fuel debts differs from that of ordinary debts in a number of ways. Restraints on diligence do not require the creditor to continue to supply goods or services to the defaulting consumer in the future; restraints on disconnection, by contrast, necessarily imply that the fuel authority will supply the energy on credit for so long as the restraint lasts. Since the authority has a monopoly of the thing supplied whereas an ordinary creditor does not have such a monopoly, it can be, and has been, argued that a restraint on disconnection would be justified.[7] Nevertheless it will be apparent that the issues are very different from the ordinary private law issues of debt enforcement, and involve the special position, financing and functions of nationalised industries, and the question whether people should have a "right to fuel", topics which for the most part fall outwith our terms of reference

[1]Electric Lighting Act 1882, s. 21; Electric Lighting Act 1909 s. 18.

[2]Gas Act 1972, Sched. 4, para. 17.

[3]National Consumer Council, Report No. 2, *Paying for Fuel*, H.M.S.O., 1976.

[4]Assisted by Mr. Jack Ashley, M.P. and Mrs. Frances Morrell.

[5]Code of Practice for domestic customers issued by the Electricity and Gas Industries (revised July 1982).

[6]See e.g. Middleton, "Paying the Poor Man's Fuel Bill" [1977] *Scolag Bulletin* 166; Neillands, "Electricity Accounts and Metering" [1982] *Scolag Bulletin* 141; Grimes, "Electricity Boards and the Consumer" [1982] *Scolag Bulletin* 154.

[7]The People's Right to Fuel Bill 1983 [Bill 66] (introduced by Mr. Dennis Canavan, M.P. under the ten-minute rule procedure and ordered to be printed on 26 January 1983) made provision *inter alia* to prevent disconnection of electricity and gas in cases of hardship and to introduce a statutory code of practice to protect people threatened with such disconnection.

and expertise. We therefore make no recommendation on the matter. Second, and on the other hand, the right of the fuel boards to enforce debts due to them for the past supply of gas or electricity is, by contrast, far more clearly a question of private law. The charges are of the nature of private law debts and enforceable as such through the court and diligence systems. We cannot see any ground upon which such debts can be distinguished from other debts and accordingly we consider that they should be subject to time to pay decrees and orders. Third, it follows from the foregoing that restraints on ordinary diligence to enforce fuel debts would exist but would not extend under our proposals to restraints on the fuel boards' powers of disconnection.[1] Whether those restraints should be so extended, or whether other and different restraints should be introduced, is a matter for the Government and Parliament to decide and on that matter we express no opinion.

3.118 We **recommend:**

A time to pay decree and a time to pay order or interim order should not affect the right of a creditor to recover his debt by the exercise of any rights and remedies available to him (such as rights of set off, retention, lien, or recourse against cautioners; the exercise of security rights e.g. under standard securities or pledges; contractual rights to recover possession of heritable or moveable property, e.g. under hire-purchase agreements; and the rights of electricity or gas boards to disconnect supply) other than the diligences used to enforce unsecured debts and sequestration, and except as mentioned in Recommendation 3.25 below.[2]
(Recommendation 3.24; clause 11(1).)

Section D. Relationship between (a) time to pay decrees and orders and (b) time orders under the Consumer Credit Act 1974

3.119 With the coming into operation of Parts V to IX of the Consumer Credit Act 1974 on 19 May 1985,[3] new restrictions apply to creditors' rights to enforce regulated consumer credit and hire agreements, including discretionary control by the sheriff court of the creditor's enforcement proceedings.[4] The main mechanism of judicial control is a "time order" under section 129 of the 1974 Act. This may be an order giving the debtor time to remedy a non-monetary breach of the regulated agreement[5] or, what is more important for present purposes, an order under section 129(2)(*a*) providing for:

"the payment by the debtor or hirer or any surety of any sum owed under a regulated agreement or a security by such instalments, payable at such times, as the court, having regard to the means of the debtor or hirer and any surety, considers reasonable."[6]

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[1]The Oakes Report, *supra* recommended that a court order should be required before disconnection but this recommendation was rejected by the then Government.

[2]Para. 3.127.

[3]Consumer Credit Act 1974 (Commencement No. 8) Order 1983 (S.I. 1983/1551).

[4]The other forms of restriction are mandatory notice before default or other action by the creditor is taken (see footnote 4 on p. 119 below) and certain provisions to protect the debtor's family on his death.

[5]S. 129(2)(*b*), e.g. carrying out repairs or maintenance.

[6]A time order generally provides for payment of arrears due at the time when the order is made but, in the case of a hire purchase or conditional sale agreement, it may also deal with future payments due if the agreement continues in force: s. 130(2).

A time order may be made in three types of case.[1] First, where a creditor or owner in a regulated credit or hire agreement has infringed certain regulatory provisions of the 1974 Act,[2] the agreement is enforceable against the debtor or hirer on an order of the court only, (known as an enforcement order).[3] In an application for an enforcement order, the sheriff may make a time order. Second, the sheriff may make a time order on an application by a debtor or hirer *after* service on him by the creditor or owner of a default notice, a notice of termination of the agreement, or a notice of the creditor's intention during the currency of the agreement to demand earlier payment, recover possession of goods or land or treat any right of the debtor or hirer as terminated, restricted or deferred.[4] Third, the sheriff may also make a time order in an action brought by a creditor or owner to enforce a regulated agreement or any security, or recover possession of goods or land to which a regulated agreement relates. This will cover, for example, actions by a creditor for payment or actions for delivery of goods on hire or hire-purchase.

3.120 The Consumer Credit Act 1974 affects a wider range of cases in which diligence is or may be used than was regulated by the Hire Purchase (Scotland) Act 1965 and the Moneylenders Acts 1900 to 1927 which it replaces. Formerly, the main method of judicial control of the enforcement of hire purchase and conditional sale agreements was the postponed order for specific delivery, in which the sheriff could suspend the order for delivery to give time for payment by instalments and could (but need not) require the creditor to obtain the leave of the court before instructing diligence to recover unpaid instalments.[5] Formerly, the number of sheriff court delivery actions of all types (not merely for recovery of goods on hire purchase or conditional sale) disposed of annually did not exceed about 1,500 as compared with about 90,000 debt actions.[6] The 1974 Act applies to a much larger number of payment actions than were covered by the Moneylenders Acts, (the numbers of which in the Scottish courts are not recorded[7]). The Consumer Credit Act 1974 seems to apply to most actions to enforce instalment credit agreements below the monetary ceiling (£15,000).[8] It applies to "running account credit" (e.g. bank overdraft, shop budget accounts, credit cards and option accounts) and "fixed sum credit" (e.g. hire purchase, conditional sale, credit sale, personal loans, bank loans, pawnbrokers' loans and check and voucher trading). But there are some very important exemptions.[9] Thus debtor-creditor-supplier agreements for fixed-sum credit are generally exempt if the number of payments

[1]S. 129(1).

[2]By entering into an improperly executed agreement or security agreement, or by failing to serve a copy notice on a surety, or by taking a negotiable instrument as security: ss. 65(1); 105(7)(*a*), (*b*); 111(2); 124(1), (2).

[3]Ss. 127, 189(1).

[4]See s. 87 (default notices); s. 98(1) (notice of termination of regulated agreement); s. 76 (notice of creditor's intention to take certain steps during currency of agreement).

[5]Hire-Purchase (Scotland) Act 1965, s. 38(4).

[6]*Civil Judicial Statistics Scotland 1982* Tables 3.4, 3.7, 9 and 10.

[7]In England and Wales, in 1983, the number of moneylenders' claims (except under a mortgage) numbered 32,680. *Judicial Statistics 1983* Table 7.3.

[8]1974 Act, s. 8(2) (consumer credit agreements); Consumer Credit (Increase of Monetary Limits) Order 1983 (S.I. 1983/1878). The Act also applies to regulated consumer hire agreements where the payments do not exceed £15,000: 1974 Act, s. 15(1).

[9]1974 Act, s. 16: Consumer Credit (Exempt Agreements) Order 1980 (S.I. 1980/52) as amended.

to be made does not exceed four.[1] This exempts the normal credit arrangements given by department stores e.g. budget accounts when the debtor is sent a monthly statement and must settle the debit balance by a single payment. A running account credit agreement providing for payment in relation to specified periods is exempt if it requires that the number of payments to be made in repayment of the credit provided in each period shall not exceed one.[2] This exempts for example gas, electricity and telephone accounts, and such normal monthly and weekly accounts as milkman's and newsagent's accounts. So, too, the ordinary case where a tradesman or professional person does work and bills the customer or client later is also exempt. The very large volume of public sector debt, which recently accounted for about half of all debt cases in which the debt was enforced by ordinary and summary warrant diligence, (i.e. adding together decrees in favour of the gas and electricity boards, the Post Office-Scottish Telecommunications Board, public sector landlords recovering rent arrears, and regional councils recovering rates arrears[3]) is excluded from the 1974 Act. Of the remaining volume of "decree debt", a very substantial but unquantifiable proportion is also excluded.

3.121 The coexistence of the 1974 Act system of time orders on the one hand and the system of time to pay decrees and orders on the other hand raises certain issues. First, in cases where actions are brought to enforce regulated agreements or related securities (e.g. cautionary obligations) within the meaning of the 1974 Act, the courts will have power to make a time order under section 129(2)(*a*) of that Act and a different power to make a time to pay decree under our recommendations. The availability of two different types of order may confuse defenders in debt actions enforcing regulated agreements and related securities,[4] and we considered whether the general power to make time to pay decrees in court actions for payment should apply only in cases where time orders under the 1974 Act are not competent. Such a solution however, would unnecessarily cause even worse problems, e.g. if the debtor mistakenly applied for the wrong type of order. We propose therefore that in such actions it should be competent for the debtor to apply either for a time order under the 1974 Act or a time to pay decree.

3.122 Second, it appears to be possible for a creditor to raise an action to constitute a debt due under a regulated agreement or related security after the debtor has already obtained a time order under the 1974 Act, e.g. in a prior application by the creditor for an enforcement order under the 1974 Act[5] or on a prior application by the debtor for a time order.[6] It is also possible that the debtor might apply for a time to pay order when he had already obtained a time order under the 1974 Act. Conversely, where the debtor had obtained a time to pay decree or order, he might also apply subsequently for a time order under the 1974 Act. Since time orders or ancillary orders under the 1974 Act can stop enforcement of debts by repossession of property,

[1]1980 Order, article 3(1)(*a*)(i).

[2]1980 Order, article 3(1)(*a*)(ii).

[3]See the O.P.C.S. Defenders Survey, p. 17, Table 3.3; cf. the C.R.U. Court Survey, para. 1.2 (which does not cover summary warrant diligence).

[4]This is not a problem created by our recommendations but already exists given the overlap of summary cause instalment decrees and time orders.

[5]1974 Act, ss. 127, 128, 129(1)(*a*).

[6]1974 Act, s. 129(1)(*b*).

realisation of secured property, recourse against cautioners and the like as well as enforcement by the ordinary modes of diligence, the debtor must clearly have the option of applying for such orders.

3.123 These possibilities create the risk that payment of the debt could be regulated simultaneously by different and inconsistent orders. Clearly therefore it should be incompetent to grant a time to pay decree or order while a time order is in force, and *vice versa*. Apart from double regulation, however, there is a risk that a debtor might seek to rely successively on time to pay decrees or orders and also on time orders whether in that sequence or the reverse sequence. This, we think, would be unfair to creditors. Partly for this reason and partly to avoid double regulation of the same debt by inconsistent orders, we propose that where a debtor had obtained a time order under the 1974 Act, then, whether or not the time order was still in force, it should not be competent thereafter for the sheriff to grant a time to pay decree or order for the same debt under our recommended legislation. Conversely, it should be incompetent to grant a time order where a time to pay decree or order had been granted relating to the same debt. To assist the court in applying these requirements, we think that provision should be made by act of sederunt to ensure that the applicant for a time order should inform the court that no previous time to pay direction or order had been made; that an applicant for a time to pay order should inform the court that no prior time order had been made; and that a creditor or owner pursuing an action to enforce a regulated agreement or related security should lodge in court a copy of any previous time order relating to the debt. We note that in a case where the sheriff may make a time order both for arrears and for future payments under a regulated hire purchase or conditional sale agreement,[1] a time to pay decree or order may already have been made for the arrears or a proportion thereof. The future payments are in effect new debts and we think that a time order should be competent in relation to them.[2]

3.124 Third, for no very clear reason (except perhaps the circumstance that the Act of 1974 was largely framed against the background of a different system of law), the system of judicial control through time orders and enforcement orders under the Consumer Credit Act 1974 does not make express provision for the case where the regulated agreement or related security agreement has been registered in the books of court for preservation and execution and accordingly where the creditor has a warrant for summary diligence, i.e. can execute diligence without constituting his debt in a court action. It seems likely that, in such a case, the debtor may lose the opportunity to apply for a time order because there will be no court action and therefore no summons which might alert him to the need to apply for a time order.[3] If diligence had been commenced, it is not at all clear that the court could grant a time order under the 1974 Act sisting diligence.

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[1]1974 Act, s. 130(2).

[2]This, we think, would be the effect of the new subsection (3) to be inserted in section 129 of the Consumer Credit Act 1974 by para. 20(*b*) of Schedule 7 to the Bill annexed to this report.

[3]Provision however is not at present made by act of sederunt requiring that the summons in an action to enforce a regulated agreement or related security should inform the defender of his right to apply for a time order in contrast to the rules in summary cause actions for payment providing for simple forms of application for an instalment decree.

3.125 To avoid these unfortunate results, we suggest that summary diligence should be made incompetent as a means of enforcing payment under a consumer credit or consumer hire agreement or related "security" (e.g. a cautionary obligation). Under older legislation, summary diligence was incompetent in the case of moneylenders' agreements.[1] Under the 1974 Act, summary diligence on negotiable instruments will not occur since a creditor or owner cannot take such an instrument (other than a cheque or bank note) in payment of a sum due under a regulated consumer credit or hire agreement by the debtor, hirer or any surety.[2] It would be a logical extension of this protection to prohibit summary diligence on all regulated agreements and related securities.

3.126 Fourth, we note that the 1974 Act does not make provision to deal with the problems arising where applications for time orders are made after diligence has commenced. It is for consideration whether the 1974 Act should be amended to make it clear that in Scotland, where diligence has reached the advanced stage at which a time to pay order would not be competent as recommended above,[3] then the court should not be entitled to make a time order until the diligence has been completed or has otherwise ceased to have effect. It is also for consideration whether when a time order is made after diligence has commenced, the court should have the same powers and duties to make orders recalling, restricting or "freezing" existing diligences as, under our recommendations,[4] it would possess in the case of time to pay orders. We have not included provisions on these lines in the Bill annexed to this report but we think that the competent authorities should consider the matter with a view to legislation.

3.127 We **recommend:**

(1) Where a time order has been made under the Consumer Credit Act 1974, it should not be competent thereafter to make a time to pay direction or time to pay order under our recommended legislation for the same debt whether or not the time order is still in operation.

(2) Conversely, where a time to pay decree or order has been granted under our recommended legislation, it should not be competent thereafter to grant a time order under the 1974 Act for the same debt whether or not the time to pay decree or order is still in operation.

(3) Provision should be made by act of sederunt requiring—

(*a*) the creditor or owner in an action brought to enforce a regulated agreement or any related security within the meaning of the 1974 Act to lodge a copy of any existing or previous time order relating to the debt;

(*b*) a debtor applying for a time to pay order to state in his application that no time order under the 1974 Act relating to the debt has been made; and

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[1]The Moneylenders Act 1927, s. 18(*h*) prohibited summary diligence on any bill of exchange, promissory note, bond or obligation granted to or held by a moneylender.

[2]S. 123.

[3]Para. 3.63; Recommendation 3.14(2).

[4]Paras. 3.85 and 3.93.

(*c*) a debtor applying for a time order under the 1974 Act to state in his application that no time to pay direction or order relating to the debt has been made under our recommended legislation.

(4) Summary diligence should be incompetent to enforce payment of a sum owed under a regulated agreement or any related security within the meaning of the 1974 Act.
(Recommendation 3.25; clause 13; Schedule 7, paragraphs 19 and 20.)

CHAPTER 4

DEBT ARRANGEMENT SCHEMES

Section A. Introduction of debt arrangement schemes

4.1 In this Chapter we advance recommendations for the introduction in the law of Scotland of a new procedure, to be called a debt arrangement scheme, designed primarily to assist a wage or salary earner or a small trader owing multiple debts to make orderly and regular payment of his debts to his several creditors. The recommendations complement our proposals in Chapter 3 for the introduction of time to pay decrees and time to pay orders which were designed to deal with single debts. Whereas time to pay decrees and orders would give a debtor an extension of time to pay, a debt arrangement scheme on the lines we recommend would give a debtor not only an extension of time to pay but also in appropriate cases a discharge of debts on payment of a composition of less than their full amounts. A debt arrangement scheme is thus not merely a "diligence-stopper" but is also in the nature of an insolvency process resembling, in this respect at least, a sequestration under bankruptcy legislation. The recommendations in this Chapter are also designed to complement the recommendations for the reform of sequestrations submitted in our Report on *Bankruptcy and Related Aspects of Insolvency and Liquidation*[1] which is being implemented with modifications by the Bankruptcy (Scotland) Bill 1984 presently before Parliament.[2] Debt arrangement schemes would differ from sequestrations in significant respects discussed later.[3]

The problem of multiple indebtedness

4.2 Every year in Scotland many thousands of ordinary wage or salary earners or small traders are or become insolvent, that is to say, unable to pay their debts as and when they fall due. Statistical measurements of the incidence of insolvency in this sense are not available but the research commissioned for this report gives helpful information on the topic. The C.R.U. Debt Counselling Survey remarked:[4]

> "Multiple debt problems (defined as difficulties with more than one bill) occur when a number of creditors are in active pursuit simultaneously. This of course does not mean that all debts have reached the same stage in recovery procedures. About 10% of debtors who come to the voluntary organisations in the survey for assistance have multiple debt problems . . .
>
> "The majority of multiple debt problems consist of two debts (60%). The incidence of cases with three debt problems is 25% of the total; those cases with four and five debt problems are 8% and 2% respectively and the remaining proportion of cases have over five debts. The sums of money involved in these multiple debts are most frequently for amounts between

[1]Scot. Law Com. No. 68 (1982).

[2]References to the Bankruptcy (Scotland) Bill 1984 are references to the Bill as brought from the House of Lords to the House of Commons, and ordered to be printed, on 18 December 1984: House of Commons, Bill 48 (1984–85).

[3]Para. 4.13.

[4]Paras. 4.10 and 4.11.

£100–400 (70%). Fifteen per cent of cases are under £100, 5% of cases between £400–500 and 10% over £500 . . . Rent-and-rates and fuel are the two types of debt occurring most frequently together."

(These sums do not reflect present levels of debts since the time of the survey was 1979.)

4.3 The O.P.C.S. Defenders Survey[1] shows that, as regards defenders in debt or debt-related actions, 69% gave as their main reason for default a simple inability to pay: of these, nearly three-quarters (74%) were having difficulty with other bills. However, as few as 15% said that court action was being taken, or was likely to be taken, over at least one. The other bills most often mentioned were electricity bills (54%), gas bills (16%), rent or mortgage payments (19%), and bills or instalment payments for goods (19%).

4.4 The Edinburgh University Debtors Survey[2] found that 49 of the 100 debtors interviewed against whom diligence had been done under a decree were in arrears for other debts. Of these 31 debtors had decrees against them for other debts; 18 were subject to one other decree; nine to two other decrees; two to three other decrees; and two to four other decrees. This finding, however, does not yield a statistical inference for all debtors subject to diligence.[3]

4.5 It seems likely that those debtors who reach the stage of diligence for one debt are more likely to be in arrears with other bills than those at the earlier stages of the debt recovery process but the O.P.C.S. Defenders Survey suggests that relatively few debtors have more than one decree operative against them at any one time. It also appears likely that, even in the case of debtors who are subjected to diligence, for a substantial number, insolvency is an isolated problem rather than a symptom of chronic indebtedness.

4.6 The research suggests that procedures are needed to enable multiple debtors to gain time to pay their debts free from the threat of diligence. The plight of a debtor subjected to diligence by one creditor may be bad enough but may be considerably worsened if he is pressed on all sides by several creditors. In Chapter 2, we saw that particular steps in diligence frequently operate as a catalyst for an instalment settlement. Where the debtor has defaulted on debts due to several creditors, he may find it difficult to enter into payment arrangements with all his creditors. Frequently, for any of a variety of possible reasons, he may not respond to invitations by his creditors to make an instalment settlement. If he simply does nothing, then his total indebtedness may be increased considerably since his several creditors may initiate separate court actions, and instruct separate diligences, for the expenses of which the debtor will ultimately be liable.

4.7 The research into debtors' circumstances commissioned for this report also throws much light on the causes of debt of ordinary wage-earners. This research suggests that in most cases of consumer insolvency or multiple debt,

[1]Section 4.2.

[2]Paras. 2.11 and 2.12.

[3]The sample of debtors was small, and was not random but was designed to focus on debtors who had experienced the final stages of diligence.

default is attributable to inability rather than unwillingness to pay: in most cases, the debtor has been unfortunate or unwise, but in no sense fraudulent or dishonest.[1] Moreover, the debtor will sometimes be unable to handle the financial crisis on his own. Most self-employed small traders and shopkeepers and others in small businesses who become insolvent are also likely to have been unfortunate or unwise, rather than dishonest, and to experience difficulty in coming to terms with their several creditors.

4.8 Moreover, multiple debt can be unfair to creditors since it can lead to an unco-ordinated race of diligences in which the practical rule of priority among competing creditors is "first come, first served". The considerate creditor, who wishes to allow the debtor time to pay, risks being shut out by the prior diligences of competing creditors.

The orderly and regular payment of debts under debt arrangement schemes

4.9 In the light of these considerations, we invited comments in our Consultative Memorandum No. 50 on detailed proposals to introduce debt arrangement schemes designed to assist insolvent wage-earners, and possibly other small debtors, in multiple indebtedness to achieve the orderly and regular payment of their debts over a reasonable period. As indicated in Chapter 2,[2] debt arrangement schemes, in the form which we now recommend, would have the following main features:

(1) an extension of time to pay all debts (in full or by way of composition) over three years with possible extension to five years;

(2) the stoppage of diligence and of petitions for sequestration by all creditors in civil debts during the life of the scheme;

(3) control by the sheriff of the making of schemes with provision for objections by creditors;

(4) the receipt and disbursement of sums due under the scheme by an "administrator" (normally the sheriff clerk) appointed by the sheriff;

(5) the ranking of all creditors' claims rateably in proportion to the amounts of their debts and the disapplication by law of the preferences applied in bankruptcy sequestrations;

(6) the possibility of court orders intercepting appropriate amounts of the debtor's earnings at source to ensure payment of the sums due to the administrator for disbursement under the scheme;

(7) no vesting of the debtor's assets in a trustee for creditors but the possibility of the debtor realising specific assets and paying the proceeds under the scheme; and

(8) in schemes providing for a composition, a discharge on payment of the composition.

We believe that debt arrangement schemes on these lines would go far to meet problems which are not adequately covered by existing procedures and arrangements or by the procedures proposed in other parts of this report. A

[1] See paras. 2.64 to 2.66 above.
[2] Para. 2.126.

brief summary of the main steps in debt arrangement scheme proceedings is set out at Table 4.A below.

Advantages of debt arrangement schemes over other existing and proposed procedures and arrangements

4.10 The other existing and proposed procedures and arrangements take the form of court procedures, or extra-judicial legal transactions, or informal voluntary arrangements.

Court procedures

4.11 There are no court procedures in Scots law which cater adequately for the small insolvent debtor in multiple debt.

4.12 *Instalment decrees.* The existing summary cause instalment decrees, and the time to pay decrees and orders which we recommended in Chapter 3 should replace them, would provide for an extension of time to pay a single debt due to a particular creditor but they cannot be readily adapted to deal

TABLE 4.A

MAIN STAGES IN DEBT ARRANGEMENT SCHEME PROCEDURE

1. Debtor lodges application (containing statement of affairs) for debt arrangement scheme in sheriff court.

2. Court checks whether application *prima facie* competent.

3. Sheriff makes (a) an order appointing administrator to prepare draft scheme and (b) an interim order sisting diligence which is served by the administrator on known creditors.

4. Administrator serves on known creditors whose debts are eligible for inclusion notices requiring them (a) to verify the amounts of their debts as at the date of service of the first of these notices ("the first notice date") and (b) to state whether interest up to that date is claimed.

5. Administrator prepares draft scheme in consultation with the debtor and serves on all known creditors and co-obligants who may acquire a right of relief against the debtor a copy of (i) the scheme application, (ii) the draft scheme, (iii) a full statement of the debtor's affairs prepared or revised by the administrator and signed by the debtor, and (iv) a notice giving the creditors and co-obligants 3 weeks within which to object.

6. If no objections are made, the sheriff must confirm the scheme. If objections are made, the sheriff must give the creditors and co-obligants an opportunity to make representations and, if agreement is not reached as to confirmation of the scheme or as to its terms, an opportunity to be heard. The sheriff then either makes an order confirming the scheme with or without modifications, or refuses the scheme application and recalls the interim sist of diligence. The scheme comes into force on the expiry of the appeal days or the disposal of an appeal upholding the confirmation of the scheme.

7. If the scheme is confirmed, the debtor makes payment to the administrator of the amounts due under the scheme, normally periodic instalments over a period of 3 years (with possible extension to 5 years in all by the sheriff on confirming or varying the scheme). The sheriff may make a pay deduction order requiring the debtor's employer to deduct from earnings and pay to the administrator all or a part of the sums due by the debtor under the scheme. The administrator makes periodic disbursements to creditors in terms of the scheme.

8. The sheriff has powers to vary or revoke a scheme on cause shown, and may vary a scheme to include new debts.

9. At the end of a successful scheme, the administrator or debtor applies for a discharge of debts, and at the same time creditors are given an opportunity to object to the discharge and, in a scheme providing for payment in full, to claim interest accrued since the first notice date. The sheriff will grant decree for payment of the interest (with or without a time to pay direction) and also grant a special type of time to pay decree relating to the unpaid balance of debts included "late" during the life of the scheme.

with debts due by a multiple debtor to his several creditors. The procedure should remain relatively simple, and uncomplicated by special provisions for ranking several creditors, for compositions, and for the collection and disbursement of payments to the creditors.

4.13 *Sequestration under bankruptcy legislation.* Under the Bankruptcy (Scotland) Act 1913, one solution for a multiple debtor whose assets did not exceed £4,000 in value was to petition for his own summary sequestration.[1] Summary sequestration provided a very effective method of defeating the claims of creditors. A petition for summary sequestration (which attracted legal aid) did not require the concurrence of creditors.[2] Creditors often did not think it worthwhile attempting to appoint a trustee in the sequestration and, in the absence of sufficient assets to provide a fee, there was no inducement for anyone to accept office as trustee. Accordingly the procedure was often abortive from the standpoint of creditors.[3] But the debtor remained immune from arrestments and poindings.[4]

4.14 To meet these and other criticisms, the Bankruptcy (Scotland) Bill 1984 (following recommendations in our report on Bankruptcy) abolishes summary sequestration, and all sequestrations follow broadly the same procedure.[5] In every sequestration, an interim trustee will be appointed (remunerated where necessary by the State)[6] and in every case the debtor will receive a discharge after three years.[7] Every petition by a debtor for his own sequestration will require the concurrence of a creditor,[8] which provides a kind of safeguard (albeit an imperfect one) against a debtor petitioning for sequestration simply to avoid diligence. We hope that these reforms will prevent abortive sequestrations and the abuse of the procedure by debtors. But these reforms mean that a debtor, who has insufficient assets to make sequestration worthwhile for his creditors, now has no court procedure which he can voluntarily initiate, without the concurrence of at least one creditor, to achieve the orderly and regular payment of his debts and a discharge on payment of a composition over a reasonable period. Debt arrangement schemes would fill that gap. We propose that a debtor would be entitled to apply for such a scheme without the concurrence of a creditor and indeed that a creditor would have no title to present such an application.

4.15 These changes in sequestration law increase the need for introducing debt arrangement schemes but, in our view, that need would still exist apart from these changes. Sequestration is an inherently expensive and complicated process which is usually not appropriate for a small debtor's insolvency. Some expense and complexity is unavoidable in any insolvency process, as our

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[1] 1913 Act, s. 174.

[2] *Ibid.*, s. 175(1).

[3] McKechnie Report, para. 304; Bankruptcy Report, para. 2.34.

[4] 1913 Act, s. 104; except arrestments and poindings used to enforce debts incurred after the date of sequestration against property or income acquired after that date.

[5] Except that there is a simplified "small assets" procedure for use where it is unlikely that the debtor's assets will be sufficient to pay any dividend to creditors of any class: Bankruptcy (Scotland) Bill 1984 clauses 20(1), 23(4) and Sched. 2: Bankruptcy Report, paras. 3.53; 7.33 to 7.36.

[6] 1984 Bill, clause 13: Bankruptcy Report, paras. 4.8 to 4.10; 7.18 to 7.28.

[7] 1984 Bill, clause 51(1): Bankruptcy Report, paras. 19.13 to 19.22.

[8] 1984 Bill, clause 5(2)(*a*); Bankruptcy Report, paras. 5.22 to 5.24.

recommendations in this Chapter indicate, but we believe that, in the normal case, a debt arrangement scheme would be a cheaper and simpler procedure than sequestration. Such a scheme would not directly interfere with property rights of the debtor, nor directly affect the property rights of third parties. There would be no meetings of creditors; no appointment of a trustee and commissioners; no vesting in the trustee of the debtor's estate; no measures to recover the debtor's property in the hands of third parties, including wrongfully alienated property; no valuation of secured, future or contingent debts; and no ranking of creditors in accordance with the rules on preferences in bankruptcy. We think that most of the complexities which would inevitably exist under our proposed debt arrangement schemes—such as the ascertainment and verification of claims; the stoppage of diligence; the disbursement of payments to creditors; the possibility of attachment of part of the debtor's earnings during the process; a procedure for the debtor's discharge—have their counterparts in sequestrations but many of the complications of sequestration would be avoided.

4.16 From the standpoint of a debtor, sequestration is a drastic remedy. If he owns his own house, he is likely to be deprived of it. He may also be deprived, subject to certain restrictions, of his household goods and effects which have become part of his daily life and which may be sold at a fraction of their use-value to him. Whether a debt arrangement scheme would avoid these consequences would depend on the terms of the scheme, but it is primarily designed to enable debts to be paid out of future income. The debtor in a sequestration may also be subjected to certain civic disabilities which a debt arrangement scheme would avoid.

4.17 The main disadvantage of a debt arrangement scheme from the debtor's standpoint is that in such a scheme he would only obtain a discharge of his debts if he completed payments under the scheme whereas, in a sequestration, the bankrupt would as of right obtain a discharge automatically after three years. The reason and justification for this difference is that a scheme is primarily designed to provide for payment out of future income, with sale of assets normally playing a small or non-existent role, whereas the rules in sequestration presuppose that the debtor has surrendered all his assets to his creditors and, in return for this surrender, is entitled to a discharge after a short period of years.

4.18 Equally from the standpoint of creditors, especially unsecured creditors who enjoy no preferences, sequestration is often a futile remedy. It is designed essentially for cases where the debtor, while possibly having considerable debts, has assets whose proceeds on sale may be divided among the creditors. But in Scotland, where most people do not own their homes, there are many insolvent small debtors who have income but no assets of any consequence available for distribution. Moreover, the lengthy procedures of sequestration are liable to diminish significantly the fund available to creditors.

4.19 In short, a debt arrangement scheme would have considerable advantages over sequestration in the case of insolvent wage-earners and small traders. It would avoid the disproportion, evident in sequestrations, between the considerable and necessary complexity and expense of the procedure and the low value of the debtor's assets.

Extra-judicial legal procedures

4.20 Scots law permits a debtor (i) to enter into a composition contract with his creditors; (ii) to grant a trust deed for his creditors; and (iii) to enter into a contract with a debt-adjuster (whereby the latter takes over liability for the debts). None of these extra-judicial arrangements are satisfactory in the case of an insolvent debtor with small assets faced with multiple debts.

4.21 *Composition contracts.*[1] Under a composition contract between a debtor and his creditors, the creditors agree to forego further diligence and to discharge their debts in consideration of the debtor paying-off, usually by instalments, a proportion of those debts. If the debtor is in business, he will usually agree to a measure of supervision of his business activities. The debtor is not divested of his whole estate (though sometimes certain assets may be conveyed in trust to a person for the benefit of the creditors).

4.22 In some limited respects, composition contracts are an ideal solution to the problems of the small multiple debtor since they embody the main principles of extension (of time to pay), composition (i.e. rateable diminution of the debts by agreed amounts), and the debtor's ultimate discharge and rehabilitation. Their great disadvantages, however, are that (even if the vast majority of creditors enter into a reasonable composition contract) no creditor can be compelled to accede to the contract, and a non-acceding creditor can continue to have diligence executed notwithstanding the contract. Recourse to composition contracts is relatively infrequent in Scotland nowadays[2] and, while we think such contracts should remain an option, their voluntary basis and unstable qualities seem to make them a quite inadequate solution to the problems of most insolvent wage-earners.

4.23 *Trust deed for creditors.* Voluntary trust deeds for creditors differ from composition contracts insofar as a trust deed involves a formal conveyance by the debtor to a trustee of his property—usually the whole of it—for the benefit of the creditors.[3] While trust deeds are popular, flexible and useful instruments when the debtor has substantial assets, they are arguably even less appropriate than composition contracts to the case of the insolvent wage-earner with few assets. As in the case of composition contracts, non-acceding creditors may frustrate the objects of the trust deed by instructing diligence[4] and a discharge of the debtor under the trust deed will not protect the debtor from diligence by non-acceding creditors. In the case of a "protected trust deed" such as will be competent under the Bankruptcy (Scotland) Bill 1984,[5] non-acceding creditors will have no higher right than acceding creditors to execute diligence during or after the subsistence of the trust deed. However,

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[1]See our Bankruptcy Report, para. 2.10 which recommended against statutory intervention applying to extra-judicial composition contracts, an approach adopted in the Bankruptcy (Scotland) Bill 1984.

[2]This may be partly because it does not bind non-acceding creditors. It is understood that, in practice, the larger companies and nationalised industries tend to stand aloof from composition contracts.

[3]Usually the purposes of the trust are simply the realisation of the debtor's estate and its proportional division among the creditors. The trust is established by a private contract between the debtor and his creditors and, for this reason, it does not bind non-acceding creditors.

[4]In relation to assets conveyed by the trust deed, diligence would require to be executed before the trustee had completed title to the property conveyed by the deed.

[5]Clause 56; Sched. 5, paras. 5–8; Bankruptcy Report, paras. 24.22 to 24.33.

a trust deed for creditors, whether it is "protected" or not, is (like sequestration) designed primarily to enable the assets of the debtor to be realised, and (again, like sequestration) where the debtor has few assets of appreciable resale value, this may operate to the serious disadvantage of the debtor without commensurate benefit to his creditors.

4.24 *Contracts with debt adjusters.* We do not know whether "debt adjustment agencies" operate in Scotland to any significant extent[1] but they certainly do not provide a widespread "private enterprise" service for insolvent consumers or wage-earners and there is no reason to suppose that they ever will.

Debt counselling and voluntary arrangements

4.25 Instead of relying on one of the foregoing legal processes, an insolvent wage-earner may turn for help to a debt counselling agency. Debt counselling can play an important role in assisting a small multiple debtor to overcome his difficulties and in selecting the most appropriate course of action available to him.[2] But arrangements for payment made as a result of debt counselling are voluntary. They presuppose the existence both of a willing debtor and willing creditors. A creditor has no assurance that the debtor will continue to pay the instalments which he has agreed to pay and refrain in the meantime from incurring further indebtedness. Further, by giving the debtor an extension of time, the creditor may find that another creditor secures payment in full by diligence. Likewise, the debtor has no assurance that one of his creditors will not terminate the informal arrangements and proceed to do diligence against his income or assets. In our view, arrangements of a mandatory character are needed such as a system of debt arrangement schemes would provide.

Consultation

4.26 There was a mixed reaction on consultation to our provisional proposals in Consultative Memorandum No. 50 to introduce debt arrangement schemes. This division of opinion stemmed in part from differing diagnoses of the scale and nature of the problem of multiple debt. In consumer debt cases, creditors do not generally perceive multiple debt as presenting problems in enforcement whereas advisers in debt counselling agencies take an opposite view.

4.27 In commenting on our Consultative Memorandum No. 50, some creditors' interests supported the introduction of debt arrangement schemes whereas the Scottish Association of Citizens Advice Bureaux, the main "generalist" debt counselling agency, while accepting that debt arrangement schemes were good in principle, expressed serious doubts about their value: the Law Society of Scotland supported the proposal while the Scottish Law Agents Society opposed it. The Society of Messengers-at-Arms and Sheriff Officers suggested that, if such schemes were to be introduced, they should be operated by officers of court under a simpler procedure.

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[1]Debt adjustment (or "pro-rating") occurs *inter alia* where a debt adjuster takes over liability for an individual's debts in return for payments from him and can be attractive to the multiple debtor since his liabilities are converted into a single debt due to the debt adjuster: see the Crowther Report para. 6.12.14. Such agencies must be licensed under the Consumer Credit Act 1974.

[2]See C.R.U. Debt Counselling Survey.

4.28 The Scottish Law Agents Society doubted whether the social considerations underlying the proposals for debt arrangement schemes would justify the introduction of such schemes. They conceded that there would be advantages in a limited number of cases. They thought there would only be a very small number of successfully completed schemes at disproportionate cost, viz:

(*a*) the cost of setting up a nationwide system of administrators suitably trained and remunerated with the necessary staff and equipment;

(*b*) a large number of detailed changes in the law and practice of bankruptcy and diligence making these matters still more complicated and introducing new possibilities for delay and expense where schemes are proposed but fail for one reason or another;

(*c*) the occupying of more court staff's and sheriff's time when already these are under severe pressure in many areas.

On consultation we had pointed that if the annual number of scheme applications were about one-tenth of the applications for County Court Act administration orders in England and Wales, there would be no more than 200 per annum.[1] If there were only a small number of applications and, of these, only a proportion were successful, then in the view of the Scottish Law Agents Society, "the proposals are not worth introducing taking everything into account and the improvements to diligence procedure discussed in other Memoranda would be adequate to deal with the general situation".

4.29 Another body whom we consulted, however, thought that the estimate of about 200 scheme applications per annum was unrealistic and that if the proposed system of debt arrangement schemes was sufficiently simple in its procedure, accessible to debtors, effective in recovering debts, and seen by consumer debtors as affording real protection from diligence, it would be widely used. We propose later certain restrictions on the competence of applications (e.g. at least one debt must have proceeded to the stage of a charge or other diligence, and the estimated product of the scheme must not fall below a minimum sum). Given that officers of court are instructed to execute diligence in about 50,000 cases annually, we believe that the foregoing estimate may indeed be unrealistically low. On the whole, we think that the advantages of debt arrangement schemes mentioned earlier outweigh the disadvantages described in the previous paragraph.

4.30 One debt collection agency, while conceding that debt arrangement schemes were "admirable" in theory, observed that in practice they would not resolve the multiple debt problem. This view was based expressly on their experience in administering a debt pooling scheme (called a "multiple account scheme") for the Scottish Retail Credit Association which apparently foundered largely because the debtors did not maintain the arrangements established under the auspices of the scheme. In our view, however, if (as we propose later) the administrator of a debt arrangement scheme can attach the debtor's earnings at source, then the likelihood of default may be much diminished.

[1] In 1978 only 1,958 applications for administration orders were made and only 1,619 orders were granted (Cmnd. 7627, Table F.1(*c*)). The numbers have recently risen. There were 3,775 administration orders granted in 1983 compared with 2,907 in 1982, an increase of 30%: Cmnd. 9370, Table 7.20.

Other legal systems

4.31 Despite the difficulties just described, we are firmly of opinion that, in principle, provision for the orderly and regular payment of debts outside bankruptcy proceedings should be available to multiple debtors, however few, who genuinely wish to meet their creditors' claims and have the means to do so within a reasonable time. Administration orders have been available in England and Wales since 1883[1] and were introduced in Northern Ireland in 1979.[2] "Summary instalment orders" closely modelled on administration orders have been introduced in New Zealand.[3] In response to the depression of the 1930s, "wage-earner plans" were introduced in the federal law of the United States of America in 1938,[4] and there have been recent law reform proposals to introduce similar legislation in the federal law of Canada[5] and Australia.[6]

4.32 Moreover, in England and Wales, the Cork Report observed that while many of their proposals were urgently needed, they had "no doubt that the most urgent need of all is for the introduction of a simple, accessible and inexpensive procedure for dealing with the ordinary consumer debtor, whose conduct does not require investigation, and who has no significant realisable assets, but who has a reasonable prospect of being able to discharge all or part of his liabilities out of future earnings surplus to his essential requirements".[7] The Cork Report recommended the introduction of a new system of debt arrangement orders (similar to our proposed debt arrangement schemes) which would replace the present County Court administration orders.[8]

4.33 Thus a study of other legal systems fortifies us in our conclusion that debt arrangement schemes would fill a gap in the provision made by Scots law for helping ordinary consumer debtors and small traders to arrange for the orderly payment of debts.

Recommendation for introduction of debt arrangement schemes

4.34 We **recommend:**

A new legal process, to be known as a debt arrangement scheme, providing

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[1]Bankruptcy Act 1883, s. 122; see now County Courts Act 1984, ss. 112–117; Administration of Justice Act 1965, s. 20; Attachment of Earnings Act 1971 ss. 4 and 5; Insolvency Act 1976, ss. 11–13; County Court Rules 1981 Order 39: see also Payne Report, paras. 737–854.

[2]Judgments Enforcement and Debts Recovery (Northern Ireland) Order 1979 (S.I. 1979/296): see now Judgments Enforcement (Northern Ireland) Order 1981 (S.I. 1981/226), articles 80 to 87.

[3]Insolvency Act 1967 (New Zealand), Part XVI.

[4]U.S. Bankruptcy Act, Chapter XIII, enacted by the Chandler Act 1938.

[5]Report of the Study Committee on *Bankruptcy and Insolvency Legislation in Canada* (the Tassé Report) (1970) Part III, Chapter 1: Ontario Law Reform Commission, Report on *The Enforcement of Judgment Debts and Related Matters* (1981) Part I, Chapter 2 on "The Orderly Payment of Debts and Instalment Payment Plans".

[6]Law Reform Commission of Australia, Report No. 6 on *Insolvency: the Regular Payment of Debts* (1977).

[7]Para. 272.

[8]Chapter 6. These proposals are not implemented by the Insolvency Bill 1984 [H.L.] (introduced on 10 December 1984) but that Bill does contain provisions, replacing deeds of arrangement, to encourage the greater use of voluntary arrangements with creditors, implementing the White Paper, *A Revised Framework for Insolvency Law* (1984) Cmnd. 9175, paras. 136–139.

for the orderly and regular payment by an individual debtor of the debts due to his several creditors should be introduced in Scots law. (Recommendation 4.1: clause 14(1).)

Section B. Content and nature of debt arrangement schemes

4.35 A debt arrangement scheme would set out the debtor's proposals for paying his creditors and would have to comply with certain statutory requirements.

Extension of time and composition

4.36 In making proposals for payment to his creditors in a debt arrangement scheme, the debtor would have three options, namely:

(*a*) an extension of time to pay his debts;
(*b*) payment of debts only to the extent of a composition, expressed as so many pence in the pound; or
(*c*) a combination of both of the above types of proposal.

4.37 A scheme providing for an extension of time for payment (with or without a composition) might, and we think normally would, provide for payment of the debt by instalments, but there would be nothing to stop a scheme providing for payment of the debts by a lump sum after a period, e.g. where the scheme required the debtor to realise specific assets and pay the proceeds to the administrator.

4.38 We think that limits should be imposed on the extension of time for payment and that in the normal case, the maximum period should be three years. We note that in England and Wales, it was at one time provided that no administration order should be made under which the payment of instalments, if kept up without default, would extend over a period of more than 10 (formerly six) years from the date of the order. Following a recommendation in the Payne Report,[1] however, the maximum duration of an administration order is now unlimited.[2] The Payne Committee argued:

> "The period of instalments payable under an administration order should, in our view, depend on the amount of the debt and the assets, means and circumstances of the debtor, and we do not think it justifiable that a debtor in comparatively modest circumstances should be refused an administration order and left at the mercy of his creditors indefinitely, whereas a man who is a proper subject for bankruptcy proceedings should be able to obtain his final discharge in due course."[3]

We do not think, however, that it is realistic to expect a scheme to have effect indefinitely or for a long period of years. We note that three years is the limit prescribed for a summary instalment order in New Zealand;[4] that it is the

[1]Para. 791.

[2]The limitation was contained in the County Court Rules 1936, Order 22, Rule 9(8) which was revoked in 1977: see now County Court Rules 1981, Order 39.

[3]Para. 791.

[4]The Insolvency Act 1967 (N.Z.) s. 146(12) provides: "No summary instalment order shall be made under which the payment of instalments if kept up without default would extend over a period of more than three years from the date of the order".

normal limit in the United States;[1] that it was accepted by the Tassé Report in Canada (who observed that "this period of time is as long as one can reasonably expect most debtors and their families to accept the discipline of the financial restrictions imposed by an arrangement")[2] and by the Australian Law Reform Commission (who remarked that "this period is believed to be an appropriate time limit if the necessary will and self-discipline of the debtor are to be maintained").[3] The Cork Report[4] observed that "the maximum duration of a [debt arrangement order] should normally be three years, but the court will have power to extend the period up to a maximum of five years, having regard to the liabilities or following a review". Moreover, we believe that in a scheme providing for a composition, a limit on the duration of the scheme would be particularly useful in assessing what level of composition would be regarded as reasonable.

4.39 On consultation, there was a mixed reaction to our proposal that a debt arrangement scheme should normally last for three years.[5] Some bodies agreed with it. One body suggested that the sheriff should be empowered to extend the recommended period and that many debtors may wish to "clear their name" even though it might take much longer than three years. One body representing creditors suggested that the period should be five years. We think, however, that the period of three years is more appropriate as the normal maximum but that the sheriff should have power to extend it for a period, but not exceeding five years in aggregate.

4.40 The possibility of discharge of debts on payment only of a composition is available in other systems which we have examined[6] and would, in our view, be essential in a system of debt arrangement schemes, especially since under the Bankruptcy (Scotland) Bill 1984 bankrupts will automatically obtain a discharge in a sequestration after three years no matter what level of composition is paid. In the case of a composition, the scheme should specify what proportion of each creditor's debt would be paid to him under the scheme.[7] It should also state the total amount payable by the debtor to all his creditors under the scheme.[8]

4.41 We **recommend:**

(1) A debt arrangement scheme should provide for:

(a) an extension of time for payment of debts; or

(b) payment of debts only to the extent of a composition; or

(c) a combination of the two foregoing types of proposal for payment.

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[1]U.S. Bankruptcy Report, p. 160.

[2]*Supra.* p. 93.

[3]A.L.R.C. Report No. 6, para. 56.

[4]Para. 313.

[5]Consultative Memorandum No. 50, Proposition 26 (para. 2.74).

[6]E.g. County Courts Act 1984, s. 112(6) (administration orders in England and Wales); Insolvency Act 1967 (New Zealand) s. 146(4) (summary instalment orders).

[7]In relation to a debt included "late", payment under the scheme means payment partly by disbursements by the administrator and partly by payments under a decree of the type proposed in Recommendation 4.17(3) (para. 4.143).

[8]*Idem.*

(2) The maximum period allowed by a debt arrangement scheme for the payment by the debtor of instalments should normally be three years from the coming into force of the scheme (when the sheriff's order confirming the scheme takes effect on the expiry of the appeal days or the disposal of an appeal).

(3) The sheriff however should have power to extend that period to be a period not exceeding five years in all. This power should be exercisable either on confirming the scheme or in an application for variation of the scheme after it has been confirmed.

(4) A scheme providing for a composition should state the proportion of each debt which the creditor in that debt would be paid, and the total amount to be paid to all creditors under the scheme.
(Recommendation 4.2; clauses 14(2), (3) and (9); 24(6) and (10); and 28(6).)

Payment of debts through administrator

4.42 We propose that a debt arrangement scheme should provide for payments to be made to the administrator (whose appointment and functions we describe later[1]) for disbursement by him to the creditors included in the scheme. The scheme would also regulate the method and times for the making of in-payments to the administrator (e.g. by instalments or deferred lump sum, whether in weekly, fortnightly or monthly periods linked perhaps to pay days; whether by the debtor himself or by his employer under the debtor's mandate; and possibly whether by bank standing order, cheque, Girocheque, cash "over the counter" or otherwise, depending on the degree of detail desired) and for disbursement by the administrator (e.g. providing for the same or different payment frequencies depending on the amounts and number of creditors involved and on possible fluctuations in the level of in-payments).

4.43 We recommend later[2] that, on or after confirming a scheme, the sheriff should be empowered to make an order requiring an employer to deduct appropriate amounts from the debtor's earnings and pay them to the administrator in order to secure so far as practicable the debtor's compliance with the scheme. To ensure that the debtor is fully apprised of this possibility, every scheme should include a statement that a pay deduction order of this type may be made. This is especially important since the amounts deducted might exceed the amounts which could be deducted by earnings arrestments or conjoined arrestment orders such as we recommend in Chapter 6.

4.44 We **recommend:**

(1) A debt arrangement scheme should provide for payment of debts through an administrator and should regulate the method and times of in-payments and disbursements.

(2) Every scheme should state expressly that a pay deduction order may be made.
(Recommendation 4.3; clause 14(4) and (7).)

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[1]Para. 4.217.
[2]Paras. 4.268 to 270.

Appropriation of specific funds and realisation of assets

4.45 A debt arrangement scheme is primarily designed to allow the debtor to pay his debts out of future income and, differing from sequestrations or voluntary trust deeds for creditors, a scheme would not by itself vest any of his property in a trustee for the benefit of the creditors. There may, however, be cases where it would be useful if the scheme were to include a provision requiring the debtor to pay specific funds, or to realise specific items of property and pay the proceeds of sale, to the administrator for disbursement to creditors under the scheme. Such a provision might be subject to conditions, for example, requiring the debtor to grant a mandate to the holder of the funds requiring him to pay them to the administrator or a mandate to a third party enabling him to uplift and realise items of the debtor's property and pay the net proceeds of sale to the administrator. A debtor should, however, be entitled to keep property which is exempt from diligence and the provision would not apply to such property.

4.46 A provision on these lines would reduce the amounts payable out of future earnings, give flexibility to schemes, and might increase their attractions to creditors who might, in the absence of such a provision, be tempted to petition for sequestration. On consultation,[1] most commentators accepted the need for such a provision, though one body opposed it on the ground that it would allow the reintroduction of warrant sales "by the back door". This objection was, however, misconceived because the scheme would not be confirmed unless the debtor agreed to it and moreover the sale would be effected informally by the debtor, or a person authorised by him, not by diligence executed by a sheriff officer or messenger-at-arms. The Cork Report proposed that a debt arrangement order such as they recommended could be made conditional on the realisation of specified assets by the debtor himself and the payment to the administrator of the net proceeds.[2] We agree with this approach, and, in consonance with the Cork Report,[3] we think that any assets to be realised should not come under the control of the administrator but that the administrator should be responsible for ensuring that the debtor complied with the provision and make a report thereon to the sheriff. If the sheriff was satisfied that the debtor had failed to comply with the provision, he would revoke the scheme.

4.47 We **recommend:**

(1) It should be competent to include in a debt arrangement scheme a provision requiring the payment to the administrator of specified funds belonging to the debtor, or the realisation of items of the debtor's property and payment of their net proceeds, to the administrator for disbursement to creditors under the scheme. The scheme could include

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[1]In our Consultative Memorandum No. 50, Proposition 27 (para. 2.79) we sought views on the question whether the court should be given power to order the sale by the administrator or the debtor of specified assets.

[2]Para. 311: at para. 275 the Report observed that though its "proposals are intended to meet the requirements of the debtor who has no substantial realisable assets, they will also be appropriate for the debtor who has assets of some value which could be realised and the proceeds paid over for the benefit of the creditors".

[3]Para. 337.

conditions designed to secure compliance with the provision e.g. by third parties acting under the debtor's mandate.

(2) The administrator should report to the sheriff on the debtor's compliance with the provision and the sheriff should be under a duty to revoke the scheme, after giving the debtor an opportunity to be heard, if he found that the debtor had not so complied.
(Recommendation 4.4; clauses 14(5) and 30(4) and (5).)

Restriction on debtor obtaining credit

4.48 Since (as we recommend later) diligence could not be competently executed during the life of a debt arrangement scheme even by a creditor whose debt had not (or not yet) been included in the scheme, the further obtaining of credit might often be unfair to the person supplying that credit in ignorance of the existence of the scheme. Bankruptcy legislation makes it an offence for an undischarged bankrupt to obtain credit above a prescribed amount without disclosing to the supplier of credit that he is an undischarged bankrupt.[1] This provision is enacted for the benefit of potential suppliers of new credit. In the case of debt arrangement schemes, however, the interests of the creditors included in the scheme as well as the suppliers of new credit have to be protected since the obtaining of further credit might endanger the success of the scheme which primarily depends on the surrender to creditors of the debtor's future free income rather than, as in sequestration, his assets. For this reason, we think that it should be possible to restrict the obtaining of credit even from a person to whom the existence of the scheme has been disclosed. We propose that it should be competent to include in a scheme a condition that the debtor should not be entitled to obtain credit above a specified amount while the scheme was in force with exceptions for any credit obtained for rent, or electricity or gas charges, for the debtor's residence and any other exceptions from the restriction (e.g. telephone bills) specified in the scheme. So far as possible we have sought to exclude criminal sanctions for breach of duties imposed in connection with debt arrangement schemes and we think that in this case the sanction for breach of the restriction should be revocation of the scheme.

4.49 We **recommend:**

(1) It should be competent to include in a scheme a restriction on the debtor obtaining credit exceeding an amount specified in the scheme but with exemptions for credit to pay rent and gas and electricity charges for the debtor's residence and any other items so specified.

(2) On the debtor's breach of the restriction, the sheriff should have power to revoke the scheme.
(Recommendation 4.5; clauses 14(6) and 30(1).)

Voluntary nature of scheme: title to apply

4.50 We propose that the debtor, but not a creditor, should have a title to apply for a debt arrangement scheme. Since a debt arrangement scheme would provide for the orderly and regular payment of debts and for fair

[1]Bankruptcy (Scotland) Bill 1984, clause 64(8) replacing Bankruptcy (Scotland) Act 1913, s. 182.

sharing of income (and in appropriate cases funds or proceeds of sale) between creditors, and would prevent diligence from being an unregulated free-for-all between competing creditors, creditors should benefit from a scheme and we considered whether creditors should have a title to apply. We think, however, that a scheme would require the full co-operation of the debtor in preparing the scheme and in operating it when it is in force. The debtor must make a full disclosure of his means and liabilities and we consider that the compulsory disclosure of means under threat of fines or imprisonment should not be permitted except in the ultimate remedy of sequestration. Moreover, once a debt arrangement scheme is made, the source of payments to creditors will normally be the debtor's earnings or other income. It is true that, as we recommend later, in-payments may be secured by a pay deduction order, but such an order would be ancillary to a scheme which the debtor had voluntarily sought. The success of a pay deduction order, like the scheme itself, would depend on whether the debtor is prepared to remain in employment and work for his creditors over an extended period. To impose a scheme on him against his will would be likely to induce him to give up his employment or leave the area where he resides.

4.51 We note that in the case of county court administration orders in England and Wales,[1] wage-earner plans in the U.S.A., and the proposed reforms of the federal law of Australia and Canada, only the debtor possesses a title to apply. The U.S. Federal Bankruptcy Commission observed that "forced participation by a debtor in a plan requiring contribution out of future income has . . . little prospect of success" and that a wage-earner's plan "requires not merely a debtor's consent but a positive determination by him and his family to live within the constraints imposed by the plan during its entire term and a will to persevere with a plan to the end".[2]

4.52 On consultation, we sought views on whether a creditor should have a title to initiate an application for a scheme with the qualification that the debtor's consent must be obtained at an early stage.[3] While this proposal did not evoke dissent, we think on reflection that it is an unnecessary complication and that few debtors who were not prepared to apply for a scheme would give their consent.

4.53 To emphasise the voluntary nature of a scheme application, the legislation should provide expressly that a debtor may withdraw his application at any stage before the sheriff has formally confirmed the draft scheme.

4.54 We **recommend:**

A debtor, but not a creditor, should have a title to apply for a debt arrangement scheme, and it should be expressly provided by statute that the debtor may withdraw his application at any time before the scheme is confirmed.

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[1]County Courts Act 1984, s. 112(1); the Payne Report's recommendation (para. 781) that a judgment creditor should have title to apply has not been implemented. (The court may however make an administration order in a creditor's application for an attachment of earnings order.) In New Zealand, creditors may apply for instalment orders.

[2]U.S. Bankruptcy Report, p. 159.

[3]Consultative Memorandum No. 50, Proposition 5 (para. 2.17).

(Recommendation 4.6; clause 14(10).)

Section C. Forum and conditions of competence of scheme applications

Forum

4.55 We propose that original jurisdiction to entertain applications for debt arrangement schemes, and to confirm, vary and revoke such schemes, should be conferred on the sheriff and that the Court of Session's role should be limited to that of a court of appeal.[1] At present, while the Court of Session has original jurisdiction in sequestration petitions concurrently with the sheriff,[2] the Court invariably remits such a petition to a sheriff.[3] We propose later that the competence of applications for debt arrangement schemes should be restricted by an upper limit (fixed initially at £10,000) on the applicant's indebtedness, and the procedure is primarily designed to be used by consumer debtors and small traders without representation by a solicitor, still less an advocate. Moreover, there is a need to ensure that the court and administrator are easily accessible to debtors, and that debtors are readily subject to supervision by the administrator. All these factors strongly suggest that jurisdiction should be exercised locally. This conclusion was approved on consultation.[4]

4.56 We **recommend:**

The sheriff court should have exclusive jurisdiction to entertain applications for debt arrangement schemes and to confirm, vary and recall such schemes (subject to appeals on questions of law to the Court of Session as recommended in Chapter 9).
(Recommendation 4.7; clauses 14(1), 19, 24, 28, 30.)

Jurisdictional competence

4.57 The European Judgments Convention expressly excludes bankruptcy and similar proceedings from its scope.[5] Likewise the Civil Jurisdiction and Judgments Act 1982 expressly provides that the rules which it enacts for the assumption of jurisdiction in Scotland[6] do not apply to "proceedings in respect of sequestration in bankruptcy; or the winding up of a company or other legal person; or proceedings in respect of a judicial arrangement or judicial composition with creditors".[7] Instead jurisdiction in sequestration petitions is regulated by the Bankruptcy (Scotland) Bill 1984, which *inter alia* gives the sheriff jurisdiction in respect of the sequestration of a debtor if he had an established place of business in the sheriffdom or was habitually resident

[1]Restricted to questions of law as recommended in Chapter 9.
[2]Bankruptcy (Scotland) Bill 1984, clause 9 replacing Bankruptcy (Scotland) Act 1913, ss. 11, 16.
[3]See now 1984 Bill, clause 15(1) and (2); cf. 1913 Act, s. 17; Bankruptcy Report, paras. 5.34 and 5.35.
[4]Consultative Memorandum No. 50, Proposition 3(2) (para. 2.5).
[5]Article 1(2) providing that the Convention shall not apply to "bankruptcy, proceedings relating to the winding-up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings".
[6]1982 Act, Sched. 8.
[7]1982 Act, Sched. 9, para. 4.

there at any time in the year immediately preceding the presentation of the petition.[1]

4.58 We propose that the sheriff should have jurisdiction to entertain a scheme application if the debtor was "domiciled" or had an established place of business at a place within the sheriff's territorial jurisdiction. By "domiciled" we mean domiciled within the meaning of the Civil Jurisdiction and Judgments Act 1982, section 41. We prefer "domicile" to the analogous concept of "habitual residence" since, once the 1982 Act comes into operation, domicile in that sense rather than habitual residence will be the connecting factor adopted in the rules for the assumption of jurisdiction in most other Scottish proceedings.[2]

4.59 Where the debtor has no domicile or established place of business in Scotland, we think that no sheriff court should have jurisdiction. In such a case, the debtor's connection with Scotland appears too tenuous for a Scottish court to make an order affecting all his debts. In these circumstances, the insolvent debtor should initiate bankruptcy or analogous proceedings elsewhere. In this respect, the jurisdictional rules would differ from those governing applications for time to pay orders, where the existence of assets in Scotland would suffice[3] since such orders affect only one debt.

4.60 We **recommend:**

Jurisdiction in debt arrangement schemes should be exercisable by the sheriff having jurisdiction over the debtor's domicile within the meaning of the Civil Jurisdiction and Judgments Act 1982, s.41, or, in the absence of a Scottish domicile, the debtor's established place of business. (Recommendation 4.8; clause 42(1), definition of "sheriff".)

Other conditions of competence and restrictions on making of schemes

4.61 Apart from rules of jurisdiction, other limits have to be set on the availability of debt arrangement schemes to protect the interests of creditors and the public purse, to avoid abuses of the procedure and to ensure that a scheme application is not made in cases where a petition for sequestration under bankruptcy legislation would be more appropriate. The limits to be discussed relate to:

(*a*) the type of applicant, e.g. whether he is an individual, or body corporate or voluntary association;

(*b*) the insolvency and number of debts of the applicant and the stage in the debt recovery process which such a debt or debts have reached;

(*c*) an upper limit on indebtedness and the possible exclusion of business debts;

(*d*) a minimum product threshold, (i.e. whether the likely product of a scheme would justify the expense and trouble in obtaining and operating the scheme);

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[1]Clause 9(1), (4) and (5): replacing 1913 Act, ss. 11 and 16 as amended.
[2]1982 Act, Sched. 8.
[3]See Recommendation 3.16(2) (para. 3.71).

(*e*) the existence of a prior sequestration petition or award; a subsisting trust deed for creditors; or a prior debt arrangement scheme or scheme application.

These limits would take the form of conditions of competence, or restrictions of a more discretionary character, which would have to be complied with *prima facie* before the merits of the application could be considered. We now consider the first four of these limits leaving till later[1] consideration of the relationship between debt arrangement schemes and other insolvency proceedings.

4.62 *Applicant to be an individual.* A debt arrangement scheme is designed to provide for the orderly and regular payment of debts of individuals (i.e. natural persons) and not trusts, bodies corporate, partnerships, or clubs or other voluntary associations. While sequestration will in future be available for such bodies (other than registered companies),[2] there is so far as we are aware no need or at least no demand for such bodies to be allowed to keep their assets and pay debts out of future income. The inclusion of such bodies would unduly complicate the legislation. We propose also that only debts for which a debtor is personally liable should be included in schemes and accordingly a scheme would not be made in respect of trusts, executries, judicial factories and the like.

4.63 *Insolvency and related requirements.* We think it should be a condition of the debtor's application that he cannot pay his debts as they fall due. This requirement was accepted on consultation. The debtor would state this fact in the prescribed form of application. Any creditor would be entitled to challenge this statement and the administrator might also challenge it if, after enquiries, it appeared to him not to be true.

4.64 In our Consultative Memorandum No. 50,[3] we suggested that an application should be competent though neither a charge to pay nor diligence had been executed and even though no decree against the debtor had been granted. The argument was that, if the debt was admitted, it would be pointless to require the debtor to await decree in an action for payment and a charge or other diligence thereon, with the concomitant expenses for which he would be liable. On reflection, however, we think it important that at least one of the debts in question should have reached the stage where diligence was imminent or had begun, i.e. (a) the debt had been constituted by a decree (or decree of registration) bearing a warrant for diligence and a charge had been served or an arrestment executed or an adjudication action raised, or else (b) a summary warrant had been granted for the recovery of rates or taxes. In the absence of such a requirement, it is likely that court resources would be expended in dealing with applications where there was no real and substantial risk of diligence: this would not make the best and most economic use of resources. We propose that the debtor must have at least three debts of which at least one debt had proceeded to the stage just mentioned. A minimum requirement of three debts, though slightly artificial or arbitrary, is desirable to give formal recognition to the fact that debt arrangement

[1]See paras. 4.299 *et seq.*
[2]Bankruptcy (Scotland) Bill 1984, clause 6.
[3]Para. 2.6.

schemes are designed for multiple debtors. Debtors having only two debts may apply for time to pay directions or orders.

4.65 We consider that the new statutory concept of apparent insolvency,[1] though it is a pre-condition of a petition for sequestration, should be neither a necessary condition, nor even a sufficient condition, of an application for a debt arrangement scheme. It should not be a necessary condition since a debtor whose funds had been arrested without a prior charge would not satisfy the requirement. Nor should it be a sufficient condition. The new statutory concept of apparent insolvency differs from notour bankruptcy insofar as apparent insolvency may be constituted not only by practical insolvency concurring with the expiry of a charge or with diligence (as in the case of notour bankruptcy[2]) but also by three other events (apart from non-Scottish insolvency proceedings). One of these events is the grant of a trust deed for creditors (concurring with practical insolvency),[3] but such a trust deed should, we think, preclude an application for a debt arrangement scheme,[4] and should therefore not be a pre-condition of an application for such a scheme. The other two events[5] do not necessarily imply that diligence is imminent and, though they may found a petition by a creditor, or by the debtor with a creditor's concurrence, for the debtor's sequestration, we do not think they should found an application by the debtor for a debt arrangement scheme.

4.66 *Upper limit on indebtedness.* We propose that debt arrangement schemes should be largely confined to consumer debtors and small traders by imposing an upper limit on the total amount of debts owed by an applicant for a scheme. In our Consultative Memorandum No. 50,[6] issued in October 1980, we proposed that the upper limit (excluding heritably secured debts) should be fixed initially at £3,000. Reaction was mixed. Some bodies (e.g. the Law Society of Scotland and the Society of Messengers-at-Arms and Sheriff Officers) thought there should be no upper limit, while the Scottish Committee of Clearing Bankers suggested a limit of £5,000. In England and Wales, the upper limit on administration orders is £5,000 (including secured debts).[7] In 1983 the Cork Report recommended an upper limit of £10,000 (of unsecured debts) for debt arrangement orders (which would replace administration orders) with some exceptions. We suggest that a limit of £10,000 (excluding heritably secured debts) would be appropriate with a power to alter the limit by statutory instrument to keep pace with inflation. Unless heritably secured debts were disregarded when applying the limit, many owner-occupiers would be debarred from even applying for a scheme.

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[1]Bankruptcy (Scotland) Bill 1984, clause 7.

[2]Bankruptcy (Scotland) Act 1913, s. 5.

[3]1984 Bill, clause 7(1)(*c*)(i).

[4]See para. 4.302 and Recommendation 4.46(2) (para. 4.311).

[5]Namely, written notice by the debtor to his creditors that he has ceased to pay his debts in the ordinary course of business (*ibid.*, clause 7(1)(*b*)) and a creditor's demand for payment of a debt of £750 or more coupled with the debtor's failure to pay, or to deny liability, within three weeks of the demand (*ibid.*, clause 7(1)(*d*)).

[6]Proposition 4(*c*) (para. 2.13).

[7]County Courts Act 1984, s. 112; County Courts (Administration Order Jurisdiction) Order 1981 (S.I. 1981/1122).

4.67 In the absence of special provision, difficulties could arise if the upper monetary limit had to be applied rigidly with the possibility that schemes would be treated as invalid where debts had been omitted or computed erroneously. We propose that a scheme should be incompetent only if it appeared to the sheriff that the limit had been exceeded. Once an administrator had been appointed, and the error came to light, a scheme application would be refused only if the upper monetary limit had been exceeded "to a substantial extent".

4.68 *Business debts.* In our Consultative Memorandum No. 50,[1] we sought views on whether a debt arrangement scheme should be incompetent if the debts consisted of or included "business debts" (i.e. debts incurred in the course of a profession, trade or business). The Scottish Committee of Clearing Bankers thought that it would not be practical to distinguish between business debts and other debts in this context. The Law Society of Scotland also thought that business debts should be included since many debtors, who get into financial difficulties through the running of a business, run such businesses part-time while in salaried or wage-earning employment. We accept these comments. A fairly low limit on indebtedness would have the effect of excluding many business debtors. It seems unlikely that the inclusion of business debts would induce wholesalers and others to restrict credit to small businesses; sequestration would still be available in appropriate cases, and if our recommendations were accepted, business creditors would not be postponed to preferred creditors. We propose therefore that applications should be competent in the case of business debts.

4.69 *Minimum product threshold.* As a safeguard against the unnecessary or uneconomical use of the time of court officials, we think that a lower monetary limit should be set on the competence of applications for debt arrangement schemes. There is a lower limit of £750 on the amount of the debts which qualify a creditor to petition for sequestration[2] and the Cork Report[3] proposed a similar limit in the case of their proposed debt arrangement orders, citing figures which showed that in England and Wales in 1978 only 3% of applicants for administration orders owed debts amounting to less than the then lower limit (of £200 of indebtedness) for bankruptcy petitions. We think however that this lower limit should have reference, not to the amount of the debts, but to the estimated product which the scheme would be likely to yield for creditors over the proposed statutory period of three years. Although the scheme's product would be more difficult to assess than the amount of the debts, it is not the amount of the debts, but the product, which would determine whether the scheme was worthwhile.

4.70 The product of the scheme would be determined by the debtor's free income (i.e. after meeting liabilities in respect of his daily needs) over the statutory period and his other available resources. A realistic budget for the statutory period would have to be framed and this would normally involve broad estimates of the likely surplus income and other assets. The test should

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[1]Proposition 4(*d*) (para. 2.13).

[2]Bankruptcy (Scotland) Bill 1984, clause 5(4), replacing Bankruptcy (Scotland) Act 1913, s. 12 as amended by the Insolvency Act 1976, Sched. 1 (lower limit of £200).

[3]Paras. 285–288.

therefore not be a rigid criterion but should depend rather on whether it appeared to the sheriff that the debtor's resources, after meeting his daily needs, would produce at least a prescribed sum. The sum would necessarily be arbitrary but we suggest that £600 (i.e. £200 per annum in a three year scheme) would be appropriate. If while the application proceeded it became apparent that the scheme's product would be likely to fall short of this sum, the scheme application should be refused only if it appeared to the sheriff to be likely that the short-fall would be substantial.

4.71 As mentioned in Chapter 2,[1] it must be conceded that a minimum product threshold would create the anomaly that a discharge on payment of a composition would be available through a debt arrangement scheme to debtors who, though insolvent, have at least some income or assets while such discharges would not be available to the poorest debtors with very small assets living on very low wages or social security. The latter would be as much, if not more, in need. We think, however, that, given the scarcity of court resources, it would be unrealistic to recommend schemes which produced nothing or a negligible amount for creditors. Moreover, the important reforms of poindings, especially of household goods, and of earnings arrestments recommended later, as well as time to pay directions or orders, would give very substantial protection to the poorest debtors.

4.72 We **recommend:**

(1) Only persons who are individuals (not bodies corporate or unincorporate) should have a title to apply for a debt arrangement scheme.

(2) Only debts for which the debtor is personally liable should be included in a scheme.

(3) Debtors who are self-employed, as well as other debtors, should be entitled to apply for a scheme and debts incurred in the course of the debtor's present and previous profession, trade or business, if any, should be included in a scheme.

(4) A scheme application should be competent only if:

(*a*) the debtor is unable to pay his debts as they fall due;

(*b*) he owes not less than three debts;

(*c*) at least one of the debts has been constituted by decree and a charge to pay or arrestment has been executed or an action of adjudication has been raised, or a summary warrant for recovery of rates or taxes has been granted.

(5) A scheme application should be entertained only if it appears to the sheriff that:

(*a*) the total debts (exclusive of interest and expenses and disregarding a heritably secured debt) do not exceed a prescribed sum fixed initially at, say, £10,000 but variable by statutory instrument; and

(*b*) the product of the scheme is likely to reach a minimum prescribed sum (fixed initially at £600 but variable by statutory instrument) over three years.

(Recommendation 4.9; clauses 14(1) and (8), 17(1) and (3) to (5).)

[1]See paras. 2.127 and 2.130.

Section D. Inclusion and ranking of debts, stoppage of diligence, effect of scheme on creditors' other rights and remedies, and payments outside scheme

4.73 In this Section we discuss the inter-related rules on:

(*a*) the inclusion and ranking of debts in debt arrangement schemes;

(*b*) the stoppage of diligence against the debtor's property and income while a scheme application is pending or a scheme is in force;

(*c*) the payment of debts outside debt arrangement schemes;

(*d*) the effect of a scheme on creditors' rights and remedies other than diligence; and

(*e*) the rights and liabilities of co-obligants liable along with the debtor to pay debts.

The aim of these rules is to balance equitably the interests of the debtor and his several creditors, and also the interests of the creditors as between themselves, while at the same time paying due regard to the interests of co-obligants. We revert later to the relationship between schemes and other bankruptcy processes.[1]

4.74 The main features of our proposals may be summarised as follows.

(1) *Debts initially eligible for inclusion.* Generally debts which are presently due and payable, undisputed, and unsecured by contractual securities, at the date when creditors are first invited to verify the amount of their claims ("the first notice date") would be included in the scheme circulated to creditors in draft and confirmed by the sheriff. Such debts would be subject to the discharge of debts at the end of a successful scheme (whether by full payment or by payment of a composition if the scheme provided for a composition).

(2) *Interest* accrued after the first notice date would not be included in a scheme initially though in a scheme providing for full payment it could be claimed later by a procedure at the end of the scheme, excepted from the scheme's discharge of debts, and constituted by decree (with or without a time to pay direction such as we recommend in Chapter 3).

(3) *Debts identified, incurred or becoming eligible for inclusion between first notice date and confirmation.* Debts which became eligible for inclusion in the period between the first notice date and the sheriff's confirmation of the scheme would normally be included, (as where, during that period, the time for payment of a future or contingent debt had arrived, or a disputed debt was admitted by the debtor or constituted by court decree, or a debt challenged as due under an extortionate credit agreement was upheld by the court in whole or in part, or a debt formerly secured by a contractual security ceased to be so secured). Debts which had been overlooked but were identified, and debts which were incurred, during that period would normally also be included in the scheme as confirmed. Inclusion, however, would not be allowed if the application for the scheme had attained such an advanced stage that, in the sheriff's opinion, inclusion would

[1]Para. 4.299.

be more conveniently considered in a later application to the sheriff, after confirmation of the scheme, to vary the scheme by including the debt. The amount of the debt included between the first notice date and confirmation would be fixed by reference to the date when the administrator ascertained that the debt existed and was eligible for inclusion.

(4) *Pari passu ranking*. Creditors initially included in a scheme would all rank *pari passu* (rateably), i.e. in a composition scheme, each creditor would receive the same proportion of his debt as every other creditor. Creditors would also rank *pari passu* on each disbursement under the scheme.

(5) *No categories of preferential or postponed debts*. It follows that, unlike sequestrations under bankruptcy legislation, there would be no categories of preferred or postponed creditors.

(6) *Inclusion of debts by variation of confirmed scheme*. While a scheme was in force, the sheriff would have a discretionary power, on a creditor's application, to vary a scheme by including a debt which had been omitted from the scheme in error, or had been a future, contingent, disputed or secured debt at the first notice date which subsequently became payable, undisputed, or unsecured, or was a newly incurred debt. The effect would be that once the circumstances requiring or causing the exclusion of the omitted debt no longer obtained, the creditor would have the options of applying for late inclusion, or staying out of the scheme and enforcing his debt in full after its termination. In extreme cases, the sheriff might revoke the scheme on an application by an omitted creditor.

(7) *Ranking of debts included by variation*. Where a debt was included late by variation order while a scheme was in force, the creditor would rank on particular disbursements *pari passu* with the other creditors included from the beginning. The amounts of those other creditors' debts would generally be fixed by reference to the first notice date and the "late" creditor's debt by reference to the date of application for inclusion. Since he would receive fewer disbursements than other creditors, there would be an unpaid balance due to him at the end of the scheme which would be excepted from the scheme's discharge of debts and would be constituted by decree with a time to pay direction. In a scheme providing for a composition, the time to pay direction in the decree would provide for the unpaid balance of the composition (not the whole debt) to be payable by instalments or deferred lump sum which, if complied with, would discharge the debt; but if the time to pay direction lapsed on default, the unpaid balance of the whole debt would become payable.

(8) *Interim order "sisting" diligence*. At an early stage of a scheme application, the sheriff would make an interim order preventing the execution of earnings arrestments, and further procedure in a poinding (if not already followed by warrant of sale before the first notice date) and in an ordinary arrestment (if not followed by decree of furthcoming or sale before that date) pending disposal of the application. Earnings

arrestments and conjoined arrestment orders[1] would not be affected by the interim sist.

(9) *Effect of scheme on diligence.* While a scheme was in operation, it would be incompetent for any creditor, whether or not he was included in the scheme, to execute any of the ordinary diligences for the enforcement of unsecured debts. The confirmation of a scheme would have the effect of rendering ineffectual existing ordinary diligences other than (a) adjudications, and (b) any poindings and arrestments not affected by the interim order (because at the first notice date a warrant of sale or decree of furthcoming or sale had already been granted). After confirmation of a scheme, the net sums recovered after the first notice date by ordinary diligence (poinding and sale, arrestment and furthcoming or sale, earnings arrestment or conjoined arrestment order) would be treated as payments to account of the amount due to the creditor under the scheme, and any excess over that amount so recovered by the creditor would be payable by him to the administrator for disbursement to creditors under the scheme.

(10) *Secured debts.* A debt secured by a contractual security over the debtor's property (e.g. a heritable security or pledge) would not be included in a scheme unless and until the debt ceased to be secured: i.e. the creditor discharged his security, or realised the security subjects, or acquired them in partial satisfaction of the debt.

(11) *"Security diligences" and adjudications.* Debts enforceable by the "security diligences" of sequestration for rent or feuduty or of poinding of the ground, and (for different reasons) debts secured by adjudications, would be treated in much the same way as debts secured by contractual securities.

(12) Arrears of *maintenance* (aliment and periodical allowance on divorce) accrued before the first notice date would be included but arrears of maintenance accruing thereafter would not be included. While a scheme was in force, maintenance would not be enforceable by a current maintenance arrestment or other diligence.

(13) *Debts due under court orders in criminal proceedings* (including fines and compensation orders) would continue to be enforceable outside the scheme.

(14) *A co-obligant of the debtor*, including a cautioner (guarantor), who by a partial payment of the debt had acquired a right of relief against the debtor before the first notice date would be included in the scheme as a creditor in his own right. Where payment of the balance of the whole debt (not the composition) was made, and the right of relief acquired, subsequently, the co-obligant could be subrogated for the original creditor by a simple procedure so that double ranking by the original creditor and co-obligant for the same debt would be avoided.

(15) A scheme would not generally affect the exercise of the *rights and remedies other than diligence available to a creditor*, such as rights of set-off; retention; lien; recourse against co-obligants; security rights;

[1]See Chapter 6.

contractual rights to recover possession of heritable property (e.g. under tenancy agreements) or moveable property (e.g. under hire purchase agreements); or the rights of the electricity and gas boards to discontinue supply. Hire purchase debts would generally not be included until the hire purchase agreement was terminated.

(16) Provision would be made regulating the relationship between *orders under the Consumer Credit Act 1974, Part IX* and debt arrangement schemes, e.g. to avoid dual and inconsistent regulation by such orders and schemes of the debtor's obligations of payment.

(17) Creditors would be safeguarded by *suspension of the running of the short and long statutory periods of prescription* of the debtor's obligation to pay debts while a scheme application or scheme subsists.

(1) Inclusion of ordinary unsecured debts

4.75 *The "first notice date"*. We propose that, so far as practicable, the amount of the debts initially included in a debt arrangement scheme should be fixed by reference to a single known date which would be the same for all of those debts. In a composition scheme, such a rule would promote equality as between the included creditors. It would be unfair if an included creditor could keep 100p in the pound of a payment made to him outside the scheme, while the other included creditors received only a dividend under the scheme. Moreover, it would unduly disrupt the procedure in a scheme application and the operation of a scheme to require adjustments of a draft scheme, or variation of a confirmed scheme, on every occasion when a payment to account of an included debt was made outside the scheme direct to the creditor. Before circulating a draft scheme to creditors, the administrator would be under a duty to serve on each of the known creditors whose debt was eligible for inclusion in the scheme a notice giving him the opportunity to verify the amount of his debt as at the date of service (by posting or otherwise) of the first of these notices served by the administrator in pursuance of this duty on a creditor. This date we have called "the first notice date". The respective shares of creditors[1] in the product of a scheme, whether it provided for payment in full or a composition, would be fixed by reference to the amounts of their debts so far as outstanding at the first notice date. Payments to account of a debt made after that date by the debtor or a third party (such as a co-obligant, relative or friend of the debtor) would not affect the amount of the debt or composition to which the creditor was entitled in terms of the scheme, though the sums actually payable by the administrator to the creditor under the scheme would be reduced by an amount equivalent to the sums paid to the creditor after the first notice date outside the scheme. For this purpose, sums recovered by a creditor by diligence after the first notice date would be treated in the same way as sums paid to the creditor outside the scheme.

4.76 A co-obligant of the debtor who, by a prior payment of the debt, had acquired a right of relief against the debtor before the first notice date would be included in the scheme as a creditor in his own right. A co-obligant acquiring a right of relief after that date would be subrogated to the creditor in the scheme by a procedure to be noted later. Only debts presently payable

[1]Other than certain creditors included "late" as described below.

(not future or contingent) and undisputed at the first notice date would be initially eligible for inclusion.[1]

4.77 *Interest.* Interest accrued on an interest-bearing unsecured debt before the first notice date would be included in the scheme but only if the interest were specifically claimed by the creditor.[2] Interest is calculated on a day-by-day basis and, especially if payments to account of a debt had been made at different times, the calculation would often be too difficult for debtors to undertake. Often creditors themselves do not seek interest on consumer debts. We propose therefore that the creditors should be given the right and opportunity to claim any interest due to them which has accrued before the first notice date at the same time as they verify the amount of their debts; the debtor should not be required to include such interest in his statement of affairs. In our Consultative Memorandum No. 50,[3] we suggested that interest accruing while the scheme application or scheme was continuing should not be payable. This suggestion met with a mixed reaction and, on reflection, we propose that, while interest should not be payable in a composition scheme, it should be payable in a scheme which provided for payment of debts in full. It should be for the creditor to claim interest accrued after the first notice date (if otherwise due by law) and we propose that each creditor should be given the opportunity to make such a claim in the procedure for discharge of debts near the end of a successful scheme providing for payment in full.[4] Interest not so claimed would be discharged by the discharge of the principal sum.

4.78 *Expenses of court actions.* As indicated in Chapter 3,[5] the procedures for obtaining and extracting decrees for court expenses vary in different courts and types of proceedings, and often a decree for expenses may be extracted a considerable time after the extract of the decree for the principal sum. We propose that court expenses should be initially included in a scheme only if a decree for expenses had been extracted, or the amount of expenses had been agreed by the debtor, before the first notice date: thus expenses found due or decerned for but not yet taxed as a quantified sum, or taxed but subject to modification on appeal, would be treated as a future, contingent or disputed debt and could be included "late" as mentioned below. We propose however that a creditor who had raised an action for payment of a principal sum against the debtor while a scheme application or scheme subsisted should only be entitled to rank in the scheme for the expenses of the action if either (*a*) the creditor was unaware of the existence of the scheme application or scheme when the action was raised, or (*b*) the creditor was so aware but the debt was disputed and required to be constituted by decree. While we believe that a scheme application or scheme should not prevent a creditor from constituting his debt by decree (against the possibility that the application or scheme might be unsuccessful and that diligence might then become necessary), we think that since for the purpose of the scheme the action was unnecessary, the creditor should bear the expenses of such an action if the application and scheme were successful. We propose therefore that where, under the foregoing

[1] As to "late" inclusion of debts becoming eligible for inclusion, see para. 4.127 *et seq.*.
[2] For secured debts, see para. 4.173.
[3] Proposition 11 (para. 2.40).
[4] See para. 4.291; Recommendation 4.44(1) (para. 4.294).
[5] Paras. 3.17 to 3.21.

rule, court expenses were excluded from a scheme because the creditor was aware of the scheme proceedings or the action related to an undisputed debt, any discharge of debts at the termination of the successful scheme should have the effect of discharging the debtor's liability for those expenses, whether or not the principal sum was discharged.[1]

4.79 *Diligence expenses.* As a general rule, the expenses of most diligences (poinding and sale, arrestment in common form, earnings arrestment, conjoined arrestment order and inhibition) incurred before the first notice date and chargeable against the debtor would be included in the debt for which the creditor ranked, unless the expenses were disputed by the debtor. Such expenses would normally be immediately quantifiable by the officer or creditor's agent. In the case of diligences which take the form of a court action, (action of furthcoming, or of adjudication[2]), only expenses agreed by the debtor, or specified as a quantified sum in an extract decree, before the first notice date would be initially included in a scheme. We discuss below[3] expenses in diligences commenced or continued after the first notice date.

4.80 We **recommend:**

(1) For the purpose of calculating the amount due to a creditor in terms of a scheme and of ranking creditors on each of the disbursements under a scheme, the amount of the debts initially included in a scheme should so far as practicable be fixed by reference to a single date occurring at an early stage of a scheme application: the proposed date is the date when the first statutory notice is served on a creditor by an administrator in the procedure recommended below for requiring creditors to verify the amounts of their debts ("the first notice date").

(2) Only debts (including interest and legal expenses) presently payable and undisputed at the first notice date would be initially eligible for inclusion in a scheme.

(3) Interest payable between the first notice date and the end of a successful scheme on an interest-bearing unsecured debt should be recoverable by the creditor only if (*a*) the scheme provided for payment of debts in full and (*b*) the interest was claimed in the procedure for discharge of debts at the end of a successful scheme as proposed below (para. 4.291).

(4) The expenses of court proceedings due by the debtor should be initially included in a scheme only if a decree for expenses had been extracted, or the amount of expenses agreed by the parties, before the first notice date.

(5) The expenses of an action for payment of a principal sum against the debtor raised while a scheme application or scheme subsisted should be included only if either (*a*) the creditor was not aware of the application or scheme when he raised the action or (*b*) the action was necessary to resolve a dispute as to liability or quantum. Where the expenses of

[1]The principal sum may not have been affected by the discharge either because it was never included in the scheme or because it was included late and, instead of being discharged, a decree was granted for the unpaid balance as proposed in Recommendation 4.17(3) (para. 4.143).

[2]An adjudging creditor would rank in a scheme only if he had discharged the adjudication.

[3]Para. 4.154.

an action were excluded in terms of this rule, and the principal sum was included in the scheme, any discharge of debts at the termination of the scheme should operate to discharge the debtor's liability for those expenses.

(6) Diligence expenses chargeable against the debtor and incurred before the first notice date should be included unless disputed by the debtor, except that the expenses of a diligence taking the form of a court action would be subject to the rule in para. (4) above.
(Recommendation 4.10; clauses 15(1)–(4), 16(2)(*a*), 29 and 39.)

(2) Ranking of creditors

4.81 *All creditors to rank* pari passu. In accordance with the rule in bankruptcy sequestrations for the ranking of creditors of the same class, we propose that creditors included in a debt arrangement scheme should rank *pari passu*, i.e. rateably according to the amount of their respective debts. In a scheme providing only for an extension of time without composition, each creditor would receive payment of his whole debt; in a scheme providing for a composition, each creditor would receive the same proportion of his debt as every other creditor. Moreover, in each disbursement to creditors under any scheme, each creditor would also rank rateably, receiving the same proportion of his debt as every other creditor.

4.82 *Debts for the supply of necessaries.* In Consultative Memorandum No. 50,[1] we sought views on whether priority should be given in debt arrangement schemes to claims for arrears due in respect of the debtor's accommodation and essential goods and services (viz. rent, secured loan interest, fuel debts and arrears of hire or hire purchase instalments of household goods required by the debtor) in order to prevent the loss of the accommodation, goods or services. This suggestion was rejected by all who commented and we agree.

4.83 We considered whether there should be categories of preferred or postponed creditors such as are provided for in sequestrations under bankruptcy legislation and in liquidations.

4.84 *No category of preferential debts.* In our Consultative Memorandum No. 50,[2] we briefly discussed the question whether debts which have a preferential status in sequestrations under bankruptcy legislation should have that status in debt arrangement schemes. This suggestion met with a divided response from consultees. Those who opposed it did not favour the principle of conceding preferential status to fiscal and other debts in insolvency proceedings but argued that the preferences in schemes should be the same as in sequestrations.

4.85 Since that time the question of preferential debts in personal and company insolvency proceedings in the United Kingdom has been widely debated. The recommendations in our Bankruptcy Report to abolish all rates and fiscal preferences in sequestrations[3] and the recommendations of the Cork

[1]Proposition 15 (para. 2.44).
[2]Para. 2.43.
[3]Chapter 15, especially paras. 15.6 to 15.24.

Report to abolish many Crown preferences in insolvency proceedings,[1] were originally rejected by the present Government[2] but following on criticisms of preferential debts made in debates in the House of Lords on the Bankruptcy (Scotland) Bill[3] and the Insolvency Bill[4] presently before Parliament, the Government stated their intention of seeking to amend those Bills so that the claims for local government rates and Inland Revenue assessed taxes (income tax, capital gains tax and development land tax) would rank as ordinary debts and so far as relevant[5] only the following debts would have preferential status,[6] viz.:

(1) *PAYE deductions* (including deductions on account of tax to certain independent contractors especially in the construction industry) which were or ought to have been made over a statutory period by the insolvent employer for the Crown under the employer's statutory duty.

(2) *Taxes and duties payable to the Board of Customs and Excise* including value added tax and car tax, and sums due in respect of general betting duty, gaming licence duty or bingo duty, for a statutory period or periods.

(3) *Social Security contributions* (viz. for financing social security benefits, the national health service and the redundancy fund) including Class 1 contributions due by employers, Class 2 by self-employed earners and Class 4 in respect of profits of a trade, profession or vocation.[7]

(4) *Occupational pension scheme contributions*: preference will be accorded to sums owed by the bankrupt to which Schedule 3 to the Social Security Pensions Act 1975 (contributions to occupational pension schemes and state scheme premiums) applies.

(5) *Wages, salaries and other benefits to employees*, i.e. pay for an amount not exceeding a sum prescribed by statutory instrument to each employee in respect of service or services rendered to the bankrupt in the four months preceding sequestration and all accrued holiday remuneration of employees.

4.86 *Employees' unpaid wages*. We think that, in some respects, the preferential status of debts due to employees has the strongest claim to recognition in debt arrangement schemes.[8] We received few comments relevant to this matter following on Consultative Memorandum No. 50 since in that Memorandum, we had proposed that schemes should only be available where the debtor was himself a wage or salary earner. Having now recommended the inclusion of business debts,[9] however, a solution must be found to the

[1]Chapter 32; especially para. 1450.

[2]White Paper, *A Revised Framework for Insolvency Law* (1984) Cmnd. 9175, para. 27.

[3]Hansard, H.L.Debs., 4 December 1984, cols. 1247–1256; 18 December 1984, cols. 539–542.

[4]Hansard, H.L.Debs., 7 February 1985, cols. 1243–1254.

[5]Since debt arrangement schemes would be competent only for living debtors, the preference for deathbed and funeral expenses in sequestrations can be ignored.

[6]At the time of writing these paragraphs, the relevant amendments had not been made to the Bankruptcy (Scotland) Bill 1984.

[7]Social Security Act 1975. The preference for Class 4 contributions is limited to a statutory period.

[8]We recommend the retention of the employee's preference in sequestrations: Bankruptcy Report, paras. 15.17 to 15.20.

[9]Recommendation 4.9(3) (para. 4.72).

problem of employees' preferential debts. As the Cork Report showed,[1] the employee's preference for unpaid wages was introduced in the early days of the Bankruptcy Acts as a social measure designed to protect a relatively poor and defenceless section of the community at a time when there was no welfare state: since then, the position of wage-earners has been greatly improved by the introduction of unemployment pay and earnings-related benefits, severance and redundancy payments, and other social security benefits. The hardship arising from delays in the payment of employees' preferential claims has been alleviated by the Employment Protection Acts under which, according to the Cork Report[2] "a substantial part, and in the majority of cases probably the whole, of each employee's claim is paid by the Secretary of State immediately out of the redundancy fund":[3] the employees' rights and remedies for recovery of the sums paid then transmit to the Secretary of State by statutory subrogation.[4] Unfortunately, the preferential debts of an employee in a sequestration are not the same as the debts which the Secretary of State is required to meet: the employee may obtain advantages from a sequestration which he would not obtain from the Secretary of State and *vice versa*.[5] We would expect that (unlike liquidations and many sequestrations), in most debt arrangement schemes, the debtor would not be an employer, and we consider that the concession of a special preferential status for employees would unduly complicate schemes without corresponding benefit. In our view, the employee should be entitled to apply for his employer's sequestration but, if he did not do so and a scheme was confirmed, the employee should rank for unpaid wages *pari passu* with other creditors. The Cork Report[6] claimed that it was unnecessarily complicated that there should be different financial and other limits on employees' preferential claims for wages in sequestrations and on rights to benefits from the redundancy fund. In the long term the solution may lie in harmonising the two codes or, as the Cork Report proposed, in the repeal of the employee's preferential status in bankruptcy coupled with an extension of the protection under the Employment Protection Acts so that no employee is worse off as a result of the repeal.[7]

4.87 Meanwhile, if we are right in thinking that a special case cannot be made for giving preferential status to unpaid wages in debt arrangement schemes, the next question is whether generally all debts having preferential status in sequestrations should be accorded that status in such schemes.

4.88 *Options on preferential debts in debt arrangement schemes.* We have considered four possible ways of dealing with preferential debts namely:

(*a*) that the preferred creditors should be excluded from debt arrangement schemes either altogether or in respect of their preferential debts and

[1]Para. 1428.
[2]Para. 1429.
[3]Employment Protection (Consolidation) Act 1978, s. 122.
[4]*Ibid.*, s. 125.
[5]See our Bankruptcy Report, para. 15.19. In the case of the employees' preferential claim in respect of contributions to occupational pension schemes, the Employment Protection (Consolidation) Act 1978, s. 123 provides for payment of those contributions where non-payment has resulted from insolvency.
[6]Para. 1431.
[7]Paras. 1431–1433.

should be entitled to enforce their excluded debts by diligence during the currency of the scheme; or

(*b*) that the preferences should apply in debt arrangement schemes; or

(*c*) that the preferred creditors should participate in a debt arrangement scheme and should rank equally with ordinary unsecured creditors but the discharge of the debts on the termination of a successful scheme would not discharge the unpaid balance of the preferential debts; or

(*d*) that the preferred creditors should rank equally with ordinary unsecured creditors in debt arrangement schemes so that debts having a preferential status in sequestrations would not have that status in debt arrangement schemes.

4.89 The first option appears to us to be the least satisfactory. It would prejudice the operation of those debt arrangement schemes where there were preferred creditors and it would not always be satisfactory for the preferred creditors themselves, since they might compete with each other in a race of diligences in a situation which requires regulation and control of enforcement to achieve the regular and orderly payment of debts.

4.90 The second option would require that provision should be made in a debt arrangement scheme for the preferred creditors to be paid in full first and, on these debts being paid, the remaining funds, if any, would be shared between the ordinary creditors amounting either to payment in full or more probably a dividend. On consultation, this option was supported by the Law Society of Scotland, who observed that there are very few bankruptcy sequestrations in which the greater part of the assets are not ultimately distributed to secured and preferred creditors, and took the view that similar considerations would apply in debt arrangement schemes. They therefore argued that it should be possible for a debt arrangement scheme to provide for payment in full to preferred creditors out of the monies payable to the administrator, and a dividend, or as the case may be, payment in full, to ordinary creditors thereafter. In the Society's view, a failure so to provide would be likely to produce a situation where a debt arrangement scheme would proceed in only a limited number of cases since preferred creditors would always object to schemes or petition for sequestration.

4.91 The main disadvantage of the Law Society's proposal is that the concession of bankruptcy preferences would complicate the framing and administration of debt arrangement schemes which ought to be kept relatively simple. The Law Society had envisaged that such a scheme would be prepared and operated by professional chartered accountants but, in our view, it is doubtful whether funds for that purpose could be found, except in a limited number of cases.

4.92 Under the third option, the preferential debts would be included in a scheme but the unpaid balance of any preferential debt at the termination of a successful scheme would not be covered by the discharge of debts at that time. We reject this solution because it is inconsistent with the basic policy of giving debtors so far as practicable an opportunity to pay off all their debts within the time scale of a debt arrangement scheme.

4.93 *Our recommended solution.* The fourth option, inclusion of preferential debts on a basis of equality with other included debts, is in our view the least unsatisfactory solution. The Cork Committee recommended[1] that, in order to keep the proceedings in debt arrangement orders simple and to avoid complications inherent in decisions relating to such orders, there should be no preferences and all unsecured debts should rank *pari passu*. This is the current position in administration orders under the County Court Acts in England and Wales[2] and in New Zealand summary instalment orders[3] and was accepted in the Australian[4] federal legislative proposals on regular payment plans. If a debt arrangement scheme provided for payment in full, the preferred creditors would not, in our view, have strong grounds to object. Even if the scheme provided only for a composition, we think that, since debt arrangement schemes would be confined to consumer debtors and small traders and exclude bodies corporate or unincorporate, the loss to the Exchequer in foregoing their preferred status would not be great. It would, we think, be a small price to pay for the successful operation of legislation designed to assist honest consumer and small business debtors to pay their debts. While we propose that, if a preferred creditor so desired, he would be entitled to apply for the debtor's sequestration, we would hope and expect that the preferred creditors would not exercise this right frequently so as to defeat debt arrangement scheme proceedings and render the legislation inoperative. We think therefore that as a general rule the preferential debts should be treated on a basis of equality with ordinary debts.

4.94 We consider later[5] the relationship between debt arrangement schemes and sequestrations. During a scheme application, we think that any creditor should have a right, if he obtained the leave of the sheriff, to petition for the debtor's sequestration, and generally a preferred creditor would be granted leave to petition since we propose that the sheriff would be required to grant leave if a scheme would be unduly prejudicial to a creditor or class of creditors. The sheriff would, however, be required to disregard any objection to the scheme application made by the preferred creditor on the ground that he would not obtain the benefit of his preference in the scheme. Moreover, once a scheme came into force, a petition for sequestration would not be competent and any creditor would require to apply first to the sheriff for revocation of the scheme: in such an application, the sheriff would again be required to disregard any contention by the preferred creditor that in the scheme, he did not or would not have the benefit of his preference. In short, the preferred creditor would be entitled to protect his preference by petitioning (with the sheriff's leave) for sequestration before the scheme is confirmed but not by objecting to a scheme nor by applying for its revocation.

4.95 An amendment would be required to Part VII of the Employment Protection (Consolidation) Act 1978 which, as indicated above, makes provision for the payment by the Secretary of State out of the redundancy

[1]Para. 324.
[2]County Court Rules 1981, Order 39, rule 18 (except that "subsequent" creditors are deferred to pre-order creditors).
[3]Insolvency Act 1967, Part XVI (New Zealand).
[4]A.L.R.C. Report, No. 6, para. 58.
[5]See para. 4.299.

fund of certain debts (including specified arrears of pay and holiday pay) owed by an employer to an employee when the employer has become insolvent, and for the transfer to the Secretary of State of the rights and remedies of the employee in respect of money paid to the employee under Part VII. We propose that Part VII should be extended to cases where an insolvent employer obtains a debt arrangement scheme. This is a necessary safeguard for the debtor's employees. It is also necessary to avoid the risk that an employee might defeat a debt arrangement scheme by applying for his employer's sequestration, not in order to obtain his preferences under bankruptcy legislation out of his employer's estate, but rather to qualify for benefits under the 1978 Act. The Secretary of State, on providing benefits under Part VII of the 1978 Act to the employee, would become entitled to be included in the debt arrangement scheme in subrogation for the employee.

4.96 We **recommend:**

(1) In debt arrangement schemes, all included creditors should rank *pari passu* on the product of a scheme and on each disbursement by the administrator to creditors under the scheme.

(2) There should be no category of preferred creditors. In particular, no preference should be given to creditors supplying accommodation or essential goods and services to the debtor, nor to creditors having a preferential status in sequestrations under bankruptcy legislation.

(3) The sheriff should disregard any objection to an application for confirmation, or any contention in an application for revocation of a scheme, made by a creditor, who would have a preference in sequestration, to the effect that he would not obtain that preference in the scheme, but pending a scheme application such a creditor should be entitled to apply for the sheriff's leave to petition for sequestration as recommended below.[1]

(4) Part VII of the Employment Protection (Consolidation) Act 1978 (payment by Secretary of State from redundancy fund of benefits to employees of insolvent person) should apply to a debtor subject to a debt arrangement scheme, with subrogation of the Secretary of State, following payment of benefits, to the employee's ranking in the scheme. (Recommendation 4.11; clauses 16(1), 25, 30(2), Sched. 7, para. 26.)

4.97 *No category of postponed debts.* In sequestrations under bankruptcy legislation, certain creditors rank only on such estate of the bankrupt as may remain after the claims of other creditors have been satisfied. The inclusion of business creditors in debt arrangement schemes raises the question whether the claims of persons participating in the debtor's business who would be postponed in sequestration should rank after the claims of other creditors are satisfied.[2] Moreover, the spouse of a bankrupt is a postponed creditor in a sequestration in relation to a loan made by him or her to the bankrupt and in respect of his or her property inmixed with the bankrupt's property and

[1]Recommendation 4.46(4) (para. 4.311).

[2]These are creditors who have sold the goodwill of a business, or lent to a business, in consideration of a share of it or at a rate of interest varying with its profits: Partnership Act 1890, s. 3; Bankruptcy (Scotland) Bill 1984, clause 48(3)(*c*).

vesting in the trustee.[1] While the views of consultees on this matter were divided,[2] we think that, for the sake of simplicity, there should be no category of postponed creditors.

4.98 We **recommend:**

Business creditors and married persons who would be postponed creditors in a sequestration should rank in a debt arrangement scheme equally with ordinary unsecured creditors.
(Recommendation 4.12; clause 16(1).)

(3) Inclusion and ranking of debts enforced by diligence and stoppage of diligence

4.99 The rules on the stoppage of diligence, and on the ranking of debts secured by diligence, in debt arrangement schemes would necessarily differ from the corresponding rules in sequestrations. A sequestration process is both a combination of diligences against the bankrupt's property and an "action" vesting the bankrupt's property (including after-acquired property) in the trustee, all for the benefit of the general body of creditors according to their respective entitlements.[3] A debt arrangement scheme, by contrast, is primarily designed to enable debts to be paid out of the debtor's future free income and (except in relation to earnings recoverable by a pay deduction order mentioned below) should not operate as a diligence against the debtor's property nor vest that property in the administrator. Since a debt arrangement scheme would not itself operate as a diligence, it should not be treated as such for the purpose of the statutory rules equalising poindings and arrestments executed within a statutory period of the constitution of "apparent insolvency".[4] Nor do we think it desirable to replicate in debt arrangement schemes the statutory rules for the reduction of prior poindings and arrestments executed within 60 days before sequestration.[5] These are designed to secure equality among the creditors sharing the bankrupt's sequestrated property: they do not seem apt for a more simple process primarily designed for sharing the debtor's future free income among his creditors.

4.100 The rules on the stoppage of diligences by debt arrangement schemes must be so framed as to ensure, so far as possible, that creditors' diligences are not adversely affected by scheme applications which, though made by the debtor in good faith, are unsuccessful, or which are made, by a debtor having no intention of paying his debts through a scheme, merely to wreck or delay his creditors' diligences. For this reason, the rules on the stoppage of diligence by sequestration under bankruptcy legislation form an inappropriate model.

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[1]Bankruptcy (Scotland) Bill 1984, clause 48(3)(*b*) replacing Married Women's Property (Scotland) Act 1881, s. 1(4) (which applied only where the bankrupt was the husband).

[2]Consultative Memorandum No. 50, Proposition 14 (para. 2.43).

[3]Bankruptcy (Scotland) Bill 1984, clauses 30–32 and 36; cf. Bankruptcy (Scotland) Act 1913, ss. 97, 98, 103 and 104: Goudy, p. 111.

[4]1984 Bill, Sched. 7, para. 10; 1913 Act, s. 10. Similarly a debt arrangement scheme should not operate as an adjudication for the purpose of the rules on equalisation of adjudications under the Diligence Act 1661 and the Adjudications Act 1672.

[5]1984 Bill, clause 36(4); 1913 Act, s. 104.

A sequestration is normally sought by creditors rather than the debtor[1] and an award of sequestration, which is granted quickly to a creditor as of right if the debtor is "apparently insolvent" in the statutory sense, cuts down all existing diligences whatever stage they have reached and renders future diligences incompetent. By contrast, only debtors would apply for debt arrangement schemes and the confirmation of a scheme would ultimately be within the discretion of the sheriff, not granted as of right. If a scheme application had the same immediate, automatic and comprehensive effect on diligences as an award of sequestration has, creditors' diligences would frequently be wrecked or prevented by scheme applications which were unsuccessful or made in bad faith.

4.101 We propose therefore that in debt arrangement schemes the stoppage of diligence should proceed in two phases. First, the sheriff would grant an interim order having strictly defined and limited effects on diligences pending disposal of the scheme application. Second, if the application were successful, the sheriff's confirmation of the scheme would preclude all new diligences and, with a few exceptions, cut down all existing diligences. We now discuss these proposals in more detail.

(a) *Interim sist of diligence*

4.102 We propose that, on appointing an administrator, the sheriff would make an interim order sisting diligence against the debtor. As soon as practicable thereafter, the administrator would intimate a copy of the interim order to each of the known creditors (including future and contingent creditors and other creditors whose debts were not or not yet eligible for inclusion in the scheme). The order would bind the creditor from the time of intimation.

4.103 The effect of the interim order would vary according to the different types of diligences and the stages which diligences had reached. In the case of the "inchoate" diligences requiring completion by sale (poinding and sale under ordinary decrees or summary warrants, arrestment and furthcoming of moveable property, arrestment and sale of ships and other vessels) or by payment (arrestment and furthcoming of funds other than earnings), we propose that the interim order should have the same effect as an interim order in an application for a time to pay order for the same reasons.[2] The creditor would be entitled to execute the poinding or arrestment but further procedure (such as an application for, or grant of, warrant of sale; intimation of removal or sale in summary warrant poindings; a summons or decree in an action of furthcoming or sale of arrested property) would not be competent.

4.104 The new modes of continuous diligences against earnings recommended in Chapter 6 take the form of "completed" rather than "inchoate" diligences (since they require the employer to pay without decree of furthcoming) and would therefore be affected by an interim order in a different way from arrestments in common form. The interim order should render incompetent the execution of a new earnings arrestment since sums attached by the earnings

[1]Under the Bankruptcy (Scotland) Bill 1984, clause 5, a petition for sequestration by the debtor without the concurrence of a creditor will be incompetent; petitions by debtors for summary sequestration will be abolished.

[2]See para. 3.80 above.

arrestment after the first notice date would affect the amount of the disbursements payable to the creditor under the scheme. The interim order should not, however, affect an existing earnings arrestment because it would be unsatisfactory to require an employer to stop deductions and payments pending disposal of a scheme application and re-start them if the application were refused. There seems no reason why a creditor having a decree for aliment or periodical allowance on divorce should not be entitled to execute a new current maintenance arrestment, or continue to recover payments under an existing current maintenance arrestment, pending disposal of a scheme application.[1] Any advantage which the maintenance creditor would enjoy as compared with an ordinary creditor would be temporary.[2] If an earnings arrestment or current maintenance arrestment were in operation, the interim order should not prevent a creditor from applying for a new conjoined arrestment order nor affect an existing conjoined arrestment order.

4.105 The interim order should render incompetent the raising of an action of adjudication for debt.[3] We propose later that an adjudging creditor should not be included in a scheme unless and until he discharged the adjudication or the diligence is completed and there is a case for imposing no restraints on adjudication processes already commenced. We think, however, that there should be a breathing space for the debtor during which the adjudging creditor may do everything necessary to give him a title and preference in competition with other creditors, but should be restrained from entry into possession or from ejecting the debtor while he (the creditor) considers the terms of the draft scheme. We propose therefore that where an action of adjudication for debt had already been raised, the creditor should be entitled to register a notice of litigiosity in the personal registers, to obtain his extract decree, to complete title to the adjudged property and to register an abbreviate of adjudication. But no further steps should be competent while the scheme application was pending. If a case occurred in which the adjudging creditor had already obtained civil possession by virtue of a decree of maills and duties, he would be entitled to continue to draw the rents.

4.106 Since an inhibition is in principle a prohibitory diligence, an interim sist should not preclude the procedure for obtaining warrant for inhibition, executing the warrant by service on the debtor, and the registration of the inhibition and any prior notice of inhibition, nor should it affect the operation of an existing inhibition or notice pending disposal of a scheme application.

4.107 The grant of a warrant for imprisonment of a debtor for wilful default in paying aliment under the Civil Imprisonment (Scotland) Act 1882, section 4, would prejudice any chance of a scheme application being successful and on balance we think that an interim order should render such a warrant incompetent pending disposal of the scheme application.

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[1]We propose later that the maintenance creditor would not rank in a scheme for maintenance arising after the first notice date: Recommendation 4.22(1) (para. 4.168) so that sums attached by a current maintenance arrestment would not affect disbursements made to the creditor under the scheme.

[2]We propose later that a current maintenance arrestment like other diligences would be rendered ineffectual by the commencement of a scheme.

[3]The nature and incidents of adjudications for debt are described at para. 3.28 above.

4.108 We propose that where the sheriff refused a scheme application, he should at the same time make an order recalling the interim order sisting diligence, and the administrator should intimate the order to the creditors concerned. As in the case of time to pay orders,[1] the period during which an interim order precluded further steps in diligence pending a scheme application should be disregarded in calculating any period during which by law a diligence remains effective.[2]

4.109 We **recommend:**

(1) On appointing an administrator in a scheme application, the sheriff should make an interim order "sisting" diligence against the debtor.

(2) A copy of the order should be intimated as soon as practicable to each of the known creditors and should bind the creditor from the date of intimation.

(3) The interim order should have the following effects:—

(*a*) It should render incompetent the grant of a warrant of sale of poinded goods; but it should not prevent a creditor from executing a poinding in common form; (the references here are to "personal" poindings, not to the secured creditor's diligence of poinding of the ground[3]).

(*b*) It should render incompetent intimation of the sale, or removal and sale, of goods poinded under a summary warrant for rates and taxes under the procedure outlined in Chapter 7; but it should not prevent the execution of such a poinding.

(*c*) It should render incompetent the execution of an earnings arrestment but it should not affect an earnings arrestment already executed. It should neither prevent nor affect a current maintenance arrestment or a conjoined arrestment order.

(*d*) It should render incompetent the raising of an action of furthcoming or sale of arrested property or ships or the grant of decree in an action already raised, but it should not render incompetent the execution of an arrestment in common form.

(*e*) It should render incompetent the raising of an action of adjudication for debt or, if such an action had already been raised the taking of any steps (such as entry into possession, ejection of the debtor) other than the registration of a notice of litigiosity in connection with the action, the obtaining and extracting of decree, registration of an abbreviate of adjudication and the completion of title (by recording the decree in the property or personal registers). But it should not affect any steps already taken in the diligence.

(*f*) It should not render incompetent the procedure for obtaining and registering a warrant of inhibition or notice of inhibition nor affect any existing inhibition (or notices) which had already been registered.

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[1]See para. 3.84 above.
[2]As to the effect of an interim order on prescription, see para. 4.214.
[3]See paras. 4.175 and 4.176 below.

(*g*) It should render incompetent the grant of a warrant for the civil imprisonment of an aliment defaulter.

(4) Time limits on the duration of diligences should be extended by the period during which the interim order affects the diligence.
(Recommendation 4.13; clause 20(1)–(3), (5); Schedule 7, paragraph 2.)

(b) *Effect of scheme on diligences for unsecured debts, and ranking of debts enforced by such diligences*

4.110 While a debt arrangement scheme was in force, it should not be competent for any creditor[1] to execute or commence the diligences by which ordinary unsecured debts are enforced or secured, namely, a poinding and sale, whether in common form (not being a poinding of the ground by a creditor in a *debitum fundi*[2]) or under a summary warrant for recovering rates and taxes, an earnings arrestment, or an arrestment and action of furthcoming or sale, an inhibition, an action of adjudication for debt, or a charge for payment, whether the diligence was used on the dependence, in security or in execution. This prohibition should take effect when the order confirming the scheme is made, superseding the interim sist of diligence.

4.111 Further, with certain exceptions, the sheriff's order confirming the scheme should have the effect of rendering ineffectual, on the date of expiry of the appeal days or the final decision on appeal upholding the order as the case may be, any of the foregoing diligences which were in operation immediately before that date. An unexpired charge should lapse as superseded by the scheme.

4.112 *Arrestments and poindings.* Where one of the "inchoate" diligences of arrestment in common form or poinding had proceeded to an advanced stage, it would often be unsatisfactory to render the diligence ineffectual, perhaps on the eve of a warrant sale. We propose therefore that the coming into force of a scheme should not render ineffectual (1) a poinding in which a warrant of sale of poinded goods had been granted but not yet executed, or (2) a poinding under a summary warrant for recovery of rates or taxes where intimation of the dates of removal and sale, or of sale, of the poinded goods had been intimated under the procedure recommended in Chapter 7, or (3) an arrestment of moveable goods or funds where decree of furthcoming or warrant of sale had been granted but not yet executed or enforced. The scheme should, however, render ineffectual poindings and arrestments which had not reached those stages.

4.113 *Diligences against earnings.* Any existing earnings arrestment or conjoined arrestment order such as we recommend in Chapter 6 would be rendered ineffectual by a debt arrangement scheme. Intimation of the confirmation of the scheme would be made by the administrator to the employer under an earnings arrestment, and to the sheriff clerk operating a conjoined arrestment order in a different sheriff court.

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[1]Whether included in a scheme or omitted from it: for omitted creditors, see para. 4.148 below.
[2]See paras. 4.175 and 4.176 below.

4.114 *Adjudications for debt.*[1] Clearly a debt arrangement scheme should preclude the raising of any new action of adjudication for debt while the scheme was in force. Pending our review of the diligence of adjudication for debt, we think that a debt arrangement scheme should not extinguish an adjudication for debt in which decree of adjudication had already been granted, nor affect an action of adjudication for debt already commenced before the interim order sisting diligence and not yet disposed of at the time when the confirmation of the scheme took effect. An adjudication for debt might have subsisted for many years and should therefore not be cut down by a debt arrangement scheme. Unlike arrestments and poindings which, having reached an advanced stage, were not rendered ineffectual by a debt arrangement scheme, an adjudication might well not be completed during the currency of a scheme. Moreover, adjudged property is not sold but ultimately vests in the adjudging creditor unless redeemed, and the effect which such vesting has on the amount of the debt is somewhat obscure. In these circumstances, pending reform of adjudications for debt, we propose that a creditor adjudging for debt should be treated in the same way as under our recommendations a secured creditor would be treated: that is to say (1) his debt would not be included in a scheme unless and until, at the first notice date or subsequently, the creditor had abandoned his action of adjudication and, had discharged any notice of litigiosity and abbreviate of adjudication which had been registered in connection with the diligence and any decree in the action which he had already obtained and (2) the scheme would not affect any existing action or decree of adjudication for debt.

4.115 *Inhibitions.*[2] Though an inhibition is in principle a prohibitory diligence and might thus be regarded as not inconsistent with a debt arrangement scheme, we consider that a debt arrangement scheme should render incompetent the obtaining of a warrant of inhibition and the registration of the inhibition in the personal registers while the scheme is in force. This is consistent with the general policy that a debt arrangement scheme should allow the debtor to pay his debts free from the threat of diligence.

4.116 The effect of a scheme on an inhibition already registered and the inclusion and ranking of a debt secured by an inhibition raises more difficult issues. We considered whether an existing inhibition and notice of inhibition should continue in force notwithstanding the scheme. We reject this option because an inhibiting creditor might obtain a preference in a ranking process (e.g. on the surplus proceeds of sale of property sold under a heritable security) for his full debt (because his debt would not be compounded in a composition scheme until the discharge of debts at the end of a successful scheme) while poinding or arresting creditors would not receive more than a composition and in many cases their diligences would be rendered ineffectual by the scheme. Moreover, while provisions in schemes requiring the debtor to dispose of heritable property and pay the proceeds to the administrator are likely to be unusual, an inhibition would prevent the debtor from complying with such a provision: this would be inappropriate, especially where the value of the heritable property was disproportionately greater than the creditor's debt. We conclude therefore that a debt arrangement scheme should render

[1]The nature and effect of adjudications for debt are described at para. 3.28 above.
[2]The nature and effect of an inhibition are described at para. 3.29 above.

a pre-existing inhibition, and any related notice of inhibition, ineffectual. This is a different solution from that adopted in time to pay decrees and orders but the difference flows from the need (which does not arise in time to pay decrees and orders) to ensure equality between creditors who have executed diligence.

4.117 An inhibiting creditor is entitled to a preference, in a sequestration or other process of ranking over the debtor's heritable estate, over posterior creditors, i.e. other creditors whose debts were created after the registration of the inhibition.[1] This is achieved by a very complicated process, sometimes called double round ranking, which in effect results in the inhibitor being compensated, for any shortfall in his dividend out of the proceeds of the bankrupt's heritable property, at the expense of the posterior creditors.[2] As we observed in our Consultative Memorandum No. 50,[3] it is desirable that the rules of ranking of inhibitions should not have to be applied in debt arrangement schemes because of the extreme complexity of these rules. This was agreed by those who commented. Where an inhibiting creditor wished to retain the benefit of his preference, he should petition for the debtor's sequestration before the confirmation of the scheme. Before presenting his petition, the inhibiting creditor would require to obtain the leave of the sheriff dealing with the scheme application but such leave would be granted if the inhibiting creditor could show that *prima facie* the scheme was unduly prejudicial to him.

4.118 We **recommend:**

(1) A debt arrangement scheme, while in force, should render incompetent the commencement or execution of a charge for payment and any of the ordinary diligences used to enforce or secure unsecured debts, namely, poinding and sale in common form (not being a poinding of the ground) or under summary warrant, earnings arrestment, arrestment and action of furthcoming or sale, inhibition, and adjudication for debt, including diligences (arrestments and inhibitions) used on the dependence or in security as well as diligences in execution. The same prohibition should apply while the order confirming the scheme is appealable or subject to appeal.

(2) As regards diligences already commenced, the scheme should render ineffectual:

(*a*) a poinding in common form (not being a poinding of the ground) not already followed by warrant of sale;

(*b*) a summary warrant poinding not already followed by intimation of the dates of removal and sale, or of sale;

(*c*) an arrestment in common form not already followed by decree of furthcoming or sale;

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[1]Bankruptcy (Scotland) Bill 1984, clause 30(2) replacing Bankruptcy (Scotland) Act 1913, s. 97(2).

[2]Bell, *Commentaries* vol. ii, p. 346; *Baird and Brown* v. *Stirrat's Tr.* (1872) 10 M. 414; Gretton, "Inhibitions, Securities, Reductions and Multiplepoindings" (1982) 27 J.L.S.S. 13, 68.

[3]See para. 2.65.

(*d*) an earnings arrestment and a conjoined arrestment order such as are recommended in Chapter 6; and

(*e*) an inhibition.

(3) A debt arrangement scheme should not affect any action of adjudication for debt which had already been raised. An adjudging creditor's debt should be excluded from a scheme unless the creditor, at the first notice date (or subsequently in terms of the rules on "late" inclusion), had abandoned his action, discharged any notice of litigiosity or abbreviate of adjudication already registered, and discharged any decree of adjudication already obtained, as the case may be.

(4) An unexpired charge should lapse.
(Recommendation 4.14; clauses 15(9); 18(1)(*a*), 5(*a*) and (*b*) and (6).)

(c) *Clearing the registers of ineffectual inhibition and adjudication documents*

4.119 Where an existing inhibition was rendered ineffectual on the coming into force of a debt arrangement scheme, the debtor should be entitled to clear the personal registers (the Register of Inhibitions and Adjudications) by registering a notice in the prescribed form of the order confirming the scheme in those registers after the scheme had come into force.[1] The debtor would be responsible for paying the registration dues. We do not think that schemes should be registered in the personal registers automatically; there may be no existing inhibition and indeed, the debtor may have no heritable property requiring protection from future inhibitions and adjudications during the currency of a scheme.

4.120 A somewhat different problem arises in relation to (1) inhibitions and notices of inhibition[2] which, though their registration had been rendered incompetent by confirmation of a scheme, were nevertheless in fact registered in the personal registers[3] during the days for appeal against the confirmation order or during the currency of the scheme, and (2) documents connected with actions of adjudication for debt[4] whose registration in the personal or property registers was ineffectual by reason of the fact that the action had been rendered incompetent by the service of an interim order on the creditor, or (as would be more likely) by confirmation of a scheme which may not have been served on the creditor in question. We think that the debtor should not

[1]A similar procedure is adopted when an inhibition is recalled. The old practice in which the Keeper marked the inhibition as recalled (Graham Stewart, p. 572; *Encyclopaedia*, vol 8, p. 189) is no longer followed.

[2]In a case of an inhibition, the documents registered are either signeted letters of inhibition on a "bill" or fiat, or a warrant in a signeted summons or other document in an action, together with the messenger's certificate of execution against the debtor; a prior notice of inhibition may also be registered and if the letters or warrant of inhibition and certificate of execution are registered within 21 days after the recording of the notice, the inhibition has effect from the date of registration of the notice.

[3]There may be a cross-entry in the Land Register since the Keeper must enter in a Title Sheet any subsisting entry in the personal registers which is adverse to the registered interest: Land Registration (Scotland) Act 1979, s. 6(1)(*c*).

[4]Namely, a notice of litigiosity and an abbreviate of adjudication registered in the personal registers and a decree of adjudication registered in the property (Land or Sasines) registers (if the adjudged interest is capable of infeftment) or in the personal registers.

be put to the trouble and expense of an action of reduction of such documents in the Court of Session and that a simpler procedure is required.

4.121 Interim orders "sisting" diligence would only affect adjudging creditors (not inhibiting creditors) and that only if the action of adjudication had been raised after service on the creditor of the interim order. Here we think that, if the creditor refused or delayed in discharging the notice of litigiosity, abbreviate of adjudication or decree of adjudication at his own expense, the debtor should be entitled to obtain from the sheriff (on an application intimated to the creditor) an order declaring that the notice, abbreviate or decree was ineffectual. A certified copy of the order would be registrable in the personal registers and, where the document was a decree of adjudication, would also be registrable in the property registers in the usual case where the decree was registrable in the property registers. The expense of registering the order would be borne by the debtor in the first instance.

4.122 A confirmed scheme would affect creditors adjudging and inhibiting either during the days of appeal against the order confirming the scheme or during the currency of the scheme. Such creditors might not have received prior notice of the scheme. As regards the method of making schemes effective against such inhibition or adjudication documents, one option would be to enact that an inhibition or adjudication document would be rendered ineffectual only if a notice of the scheme had been registered in the personal registers before registration of the document.[1] The notice would be registrable at the debtor's option.[2] Provision would be made as to the duration and, if necessary, renewal of the abbreviate, and for its cancellation on the termination of the scheme. We doubt however whether a registration of such a notice would necessarily help either creditors seeking to register an inhibition (since they would be unlikely to search the personal registers before presenting the inhibition for registration[3]) or conveyancers transacting on the faith of the registers (since the grantee in a conveyance is normally entitled, under the grantor's agent's letter of obligation to give a clear search, to have an inhibition discharged at the grantor's or agent's expense even though the inhibition is not effective in law against the conveyance[4]). This, however, assumes that the Keeper would not himself search the personal registers and refuse to accept an inhibition rendered ineffectual by the notice: we understand that since most inhibitions are presented to the Keeper for registration personally "across the counter" rather than by post, searches to identify prior registrations of schemes would be random rather than systematic and could not be accommodated within existing arrangements and resources. Registration of a scheme would alert adjudging creditors who searched the registers before raising an action of adjudication; we propose below, however, that schemes would be registered in the register of insolvencies kept by the Accountant of Court under the Bankruptcy (Scotland) Bill 1984 and the prudent creditor seeking

[1]Compare the registration of an abbreviate of the petition and first deliverance in a sequestration: Bankruptcy (Scotland) Act 1913, s. 44; Bankruptcy (Scotland) Bill 1984, clause 14.

[2]Registration would be pointless if the debtor did not own or acquire heritable property.

[3]We understand that in practice creditors register notices of inhibition and inhibitions without first searching to ascertain whether the inhibition would be ineffectual in a question with a trustee in a sequestration who has registered an abbreviate of sequestration.

[4]*Dryburgh* v. *Gordon* (1896) 24 R. 1.

to adjudge for debt could identify a scheme application or a scheme by having a search made of that register before raising his action.

4.123 We propose that where the registration of an inhibition document was ineffectual because the registration was effected during the appeal days or the currency of the scheme, or where the registration of an adjudication document was ineffectual by reason of the commencement of the action of adjudication either after the service on the adjudging creditor of the interim order or, as the case may be, during the appeal days or the currency of the scheme, the debtor should be entitled to have the document discharged, at the creditor's expense if at the time of registration the creditor had known that registration would be ineffectual or at the debtor's expense if the creditor did not possess that knowledge at that time. A discharge at the debtor's instance would be effected by a procedure similar to that for discharging adjudication documents outlined at paragraph 4.121 above. The sheriff, on the debtor's application (intimated to the creditor) would make an order declaring that the inhibition or adjudication document was ineffectual and a certified copy of the order would be registrable in the personal registers or, in the case of a decree adjudging a registrable interest in land, the property registers. This procedure would be used where it was incumbent on the debtor to clear the records at his own expense and also where the inhibiting or adjudging creditor refused or delayed in carrying out a duty of clearing the registers at his (the creditor's) expense. In the latter case, the debtor would be entitled to recover the expense of the procedure from the creditor. To avoid further complications of debt arrangement scheme procedure, we propose that the sheriff's order would not be appealable.

4.124 We **recommend:**

(1) Where an existing inhibition was rendered ineffectual on the coming into force of a debt arrangement scheme, the debtor should be entitled to have the inhibition discharged by registering in the personal registers a notice (in a form prescribed by statutory rules) of the order confirming the scheme.

(2) The sheriff should have power, exercisable (on the debtor's application intimated to the creditor concerned) on or after confirming a debt arrangement scheme, to make an order declaring ineffectual:

(i) any inhibition or notice of inhibition which was incompetent by reason of being registered after the confirmation of the scheme; and

(ii) a notice of litigiosity, an abbreviate of adjudication or a decree of adjudication registered in connection with an action of adjudication for debt which was incompetent by reason of the raising of the action either in contravention of an interim order sisting diligence or after the confirmation of the scheme.

A certified copy of the order should be registrable in the same registers (personal or property registers) as the document concerned was registrable. The declaratory order should not be subject to appeal and should take effect only after the confirmation order is no longer appealable nor subject to an appeal.

(3) The dues of registration of the notice or certified copy presented by or on behalf of the debtor should be borne by him in the first instance.

(4) As regards liability for expenses and registration dues:

(*a*) the debtor should bear the expense of obtaining and registering a prescribed notice of the order confirming the scheme mentioned in paragraph (1) above;

(*b*) the debtor should be entitled to recover from the creditor the expense of obtaining and registering a declaratory order relating to an adjudication document which was ineffectual by reason of the raising of the action of adjudication for debt in contravention of the interim order served on the adjudging creditor; and

(*c*) where a notice of inhibition or an inhibition had been registered, or an action of adjudication for debt had been raised, after the confirmation of the scheme, the debtor should be entitled to recover from the creditor the expense of obtaining and registering a declaratory order relating to the inhibition or adjudication document only if (i) the creditor had been aware, at the time of registration of the document, that the registration would be ineffectual and (ii) the creditor had refused to discharge, or unduly delayed in discharging, the registration of the document at his own expense. (Recommendation 4.15; clause 40.)

(4) "Late" inclusion and ranking of omitted unsecured debts and stoppage of diligence enforcing such debts

4.125 *The problem of omitted debts.* Under the legislation which we propose, some unsecured debts might be omitted from a draft scheme prepared by the administrator and from the scheme as confirmed by the sheriff. We propose that some categories of debts would not be initially eligible for inclusion in a draft scheme because between the first notice date and the date of confirmation of the scheme they were future debts not yet due, or contingent, or disputed, or subject to challenge under section 139 of the Consumer Credit Act 1974 (re-opening of extortionate credit agreements). Another category of omitted debts would be debts which were eligible for inclusion between those dates but were omitted from the scheme because the debtor had failed to disclose them and the administrator and sheriff were not otherwise made aware of the debts' existence or the events rendering them eligible for inclusion. Yet another category of omitted debts would consist of debts which were newly incurred during the currency either of the scheme application or of the scheme itself ("subsequent" debts).

4.126 Each of these categories of omitted debts raises somewhat different issues from the others but common to all are the problems of whether, when and how such debts should be included and ranked in schemes and how far covered by the discharge of debts at the end of a successful scheme; and whether the rules on the stoppage of diligence should apply to the enforcement of omitted debts as well as included debts and, if so, what safeguards should be enacted to protect an omitted creditor executing diligence in justifiable ignorance of a scheme.

(a) *"Late" inclusion of excluded debts*

4.127 *Future and contingent debts.* Under bankruptcy legislation, in a sequestration a creditor is entitled to vote and rank for a future debt (not yet due) only after deduction of interest from the date of sequestration to the due date of payment.[1] Where a debt is subject to a contingency which has not yet eventuated, a creditor cannot vote or rank unless his claim is capable of valuation and is valued by the trustee or sheriff.[2] If it is not valued, the trustee will, in calculating the divisible estate for the payment of dividends, set aside funds to meet the claim. We think, however, that in a debt arrangement scheme, a future debt should not be included until the time for payment has arrived, and that a contingent debt should not be included until the contingency has been purified. The functions of valuing future and contingent debts, and of setting aside funds to meet unquantified contingent debts, would be unduly onerous for the administrator. The exclusion of future and contingent debts was generally agreed on consultation[3] and is consonant with the views of the Cork Report[4] and the Australian Law Reform Commission.[5]

4.128 Debts may arise in respect of periodic or recurring payments under a wide variety of different contracts which it is impossible to enumerate exhaustively: examples include hire, hire purchase, conditional sale, credit sale, loan agreements, insurance policies and contracts of employment or for services. In the case of certain agreements (e.g. agreements secured by contractual securities, hire purchase or conditional sale agreements, and certain regulated consumer hire agreements) we propose special rules below for the inclusion of debts.[6] In other cases, the creditor would rank for arrears accrued at the first notice date. Unless there were an irritant clause providing for the termination of the contract on insolvency, the debt arrangement scheme would not terminate the contract. The debtor would require to make up his mind whether he intended to keep up payments outside the scheme, or to default and leave creditors to rank in the scheme for sums due under the contract and to use their other contractual remedies. Continuance of payments might be justifiable if, for example, the contract were a credit sale agreement for necessaries, or even a commercial contract enabling the creditor to continue in business in a small way to earn money to pay his creditors. It should however be made clear to creditors on whom a scheme application was served that payments outside the scheme were contemplated.[7] If default occurred in sums falling due after the first notice date, the creditor would have the same rights and options as any other "subsequent creditor" to apply for late inclusion in the scheme, or for its revocation, or to stay outside the scheme and enforce the subsequent debt in full after its termination.

4.129 *Disputed debts.* Where a dispute had arisen between a creditor and the debtor as to whether the debtor was liable for a particular debt or as to

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[1]Bankruptcy (Scotland) Bill 1984, Sched. 1, para. 1(2) replacing Bankruptcy (Scotland) Act 1913, s. 48.

[2]1984 Bill, Sched. 1, para. 3, replacing 1913 Act, ss. 49 and 51.

[3]Consultative Memorandum No. 50, Proposition 25 (para. 2.71).

[4]Para. 319.

[5]A.L.R.C. Report No. 6, paras. 59 and 60.

[6]See paras. 4.169 to 4.180, 4.199 to 4.201, 4.204, 4.205 (Recommendation 4.28(2) and (5)).

[7]We suggest at para. 4.234, head (i) below that this should be explicitly mentioned in the statement of affairs served on creditors along with the scheme application and scheme.

its amount, we do not think that the administrator, or the sheriff dealing with the scheme application, should be required to determine the dispute. In some cases, e.g. an illiquid delictual claim, liability and the amount of damages could only be determined in an ordinary reparation action. Even where a debt had been constituted by decree, there could be difficult questions as to whether payment had subsequently been made in whole or in part, which could only be determined in a court action. We think therefore that any debt which at the first notice date had not been constituted by decree and in respect of which the debtor did not admit liability or quantum, should be excluded from a scheme until the debt was constituted. Moreover, where a debt had been constituted by decree but the debtor and creditor were in dispute as to the state of the debt at the first notice date, the debt should be excluded from the scheme until the dispute was resolved, whether by agreement between the parties or judicially, for example by an action of declarator. A similar proposal relating to the constitution of unconstituted debts was agreed on consultation.[1]

4.130 *Debts challenged as due under extortionate credit agreements.* Under the Consumer Credit Act 1974, if the court finds a credit bargain extortionate, it may reopen the credit agreement so as to do justice between the parties.[2] In so doing, the court may relieve the debtor or any "surety" (i.e. guarantor) from payment of any sum in excess of that fairly due and reasonable and, for that purpose, may *inter alia* set aside the whole or part of any obligation imposed on the debtor or a surety by the credit bargain or any related agreement, require payment of sums or the return of property to him, and alter the terms of the credit agreement or security instrument.[3] Jurisdiction is vested in the sheriff, and may be invoked by the debtor or surety in an application brought for that purpose in the sheriff court of the debtor's or surety's residence or place of business, or in other proceedings in any court where the amount paid or payable under the credit agreement is relevant,[4] (which proceedings could include an application for a debt arrangement scheme). The Bankruptcy (Scotland) Bill 1984, clause 58, confers on the court in a sequestration process similar powers to make, on the application of the permanent trustee, orders with respect to extortionate credit transactions entered into within three years before the date of sequestration. The permanent trustee and the undischarged bankrupt are not entitled to apply under the 1974 Act for the reopening of an extortionate credit agreement.[5]

4.131 We propose that where an application under section 139 of the 1974 Act relating to a credit agreement is pending at the first notice date, any debt due under the agreement should be excluded from the scheme subject to its possible late inclusion by the procedure for variation mentioned below.[6] The uncertainty surrounding such a debt puts it in much the same position as a disputed or contingent debt. Moreover, we do not think that the sheriff should exercise powers to reopen the credit agreement in an incidental application

[1]Consultative Memorandum No. 50, Proposition 25 (para. 2.71).
[2]1974 Act, s. 137.
[3]*Ibid.*, s. 139(2)
[4]*Ibid.*, s. 139(1).
[5]1984 Bill, clause 58(7).
[6]Para. 4.134.

in the scheme application, whether under the 1974 Act, section 139 or under separate statutory provisions modelled on the new powers introduced by the Bankruptcy (Scotland) Bill in sequestrations. Such an incidental application would unduly complicate the procedure. Furthermore, we think it would be reasonable to require a debtor, wishing to make an application under section 139, to do so before the first notice date so that debts included in the draft scheme or schemes are not subject to uncertainty and change brought about by the debtor's belated action. We propose therefore that an application under the 1974 Act, section 139 should not be competent after the first notice date in a scheme application and thereafter while the scheme application was pending or the scheme was in force.

4.132 *Exclusion of debt as ground of refusal of scheme application.* The existence of a future, contingent or disputed debt, or a debt subject to challenge under the 1974 Act, section 139, which was excluded from a scheme, might well prejudice the success of any scheme especially if the amount of the debt was substantial. We would expect that the administrator in reaching a view on whether a scheme application should proceed, and the sheriff in determining whether to confirm a scheme, would take into account future debts and, so far as practicable, contingent and disputed debts and debts challenged under the 1974 Act. If the amount of the future, contingent, disputed or challenged debt was small relative to the debtor's total liabilities, the advantage would normally lie in allowing the scheme application to proceed to confirmation leaving it to the excluded creditor to apply for late inclusion thereafter. If on the other hand the amount was material, the advantage might often lie in refusing the scheme application, leaving it to the debtor to apply again if and when the omitted debt had become eligible for inclusion.

4.133 *"Late" inclusion of future, contingent, disputed or challenged debts between first notice date and confirmation of scheme.* Though a debt which was future, contingent, disputed, or challenged as due under an extortionate credit agreement, as at the first notice date, would generally not be included in a scheme, the circumstances requiring exclusion might cease to obtain in the period between the first notice date and the sheriff's confirmation of the scheme. If the administrator was aware of the change in circumstances which rendered inclusion of the debt competent, we propose that he should normally be under a duty to include the debt in the scheme. Where the debt became eligible for inclusion after a draft of the scheme had already been circulated to creditors, the administrator would require to adjust the draft scheme by including the debt, and re-circulate the adjusted draft to creditors. A new period for objections would then be allowed. In some cases, however, inclusion might become competent only at a very late stage in the scheme application, e.g. on the day of the hearing of objections. In such a case, it could be very inconvenient and unfair to the other parties to require adjustment of the scheme to include the debt and re-circulation to creditors. Accordingly, we think that, in these circumstances, if the sheriff, having regard to the stage which the scheme application had reached, were of the opinion that inclusion would be more appropriately considered in an application after confirmation for variation of the scheme so as to include the debt, the debt should not be included in the scheme before confirmation.

4.134 *"Late" inclusion of future, contingent, disputed or challenged debts by variation of confirmed scheme.* Where a debt was excluded as future, contingent, disputed, or challenged, and thereafter became eligible for inclusion, the creditor should have the option of applying to the sheriff to vary the scheme by including the debt or of waiting till the scheme was terminated (by revocation or on discharge of the included debts) and enforcing the debt in full by diligence thereafter. He should not, however, be entitled to enforce his debt by diligence during the currency of a scheme and any such diligence should be ineffectual. In contrast to "late" inclusion of a debt before confirmation, the sheriff should have a discretion whether or not to vary the scheme so as to include the creditor if he applied for "late" inclusion. It seems unlikely that there would be many cases in which the debtor would be able to increase his payments to yield the same dividend following inclusion of a new debt. If he could, we would expect that the sheriff would include the debt virtually automatically. Otherwise, the disposal of the application would depend on all the circumstances of the case, including the effects of the inclusion on the dividends and the length of time which the scheme had yet to run. In an application to vary a scheme so as to include a debt after confirmation, we think on balance that if the aggregate amount of the debts already included and the debt sought to be included "late" exceeded to a substantial extent the financial limit (of £10,000) recommended above, the sheriff must refuse the application.[1] The creditor would have the options of applying for revocation or of enforcing his debt in full after the scheme's termination. We concede, however, that a case could be made for disapplying the financial limit altogether once a scheme was in operation.

(b) *"Late" inclusion of debts identified or incurred since first notice date*

4.135 *Unidentified debts.* Cases could occur where a creditor having an admissible claim had been wrongly omitted from the scheme through some error. Normally it would be in the debtor's interest to disclose all debts to the administrator since an omitted debt would be neither subject to any composition nor discharged under the scheme. Nevertheless the debtor might have deliberately failed to disclose the existence of the debt or he might have forgotten or overlooked it. In such cases, we think that the creditor should have the options of (a) applying for inclusion in, or revocation of, the scheme, or (b) waiting till after the scheme had terminated (whether by revocation or on discharge of the included debts) and enforcing his debt by diligence thereafter. In a composition scheme, the advantage to the creditor of the second option would be that the creditor could enforce his debt in full notwithstanding that, if his debt had been included in the scheme, he would have received only a dividend. Any diligence to recover his debt executed during the currency of the scheme should be ineffectual, but as we indicate below[2] there would be safeguards for creditors executing diligence while unaware of a scheme. Where the administrator had identified the debt between the first notice date and confirmation of the scheme, the provisions on inclusion applicable to future and contingent debts, etc. should apply. Where the scheme had been confirmed the sheriff should have power to revoke the

[1]This proposal applies also to applications for "late" inclusion of "unidentified" and "subsequent" debts discussed in paras. 4.135 to 4.137.

[2]Para. 4.147.

scheme on the application of (among others) an erroneously omitted creditor which he could exercise where, for example, the creditor established that the debtor had deliberately failed to disclose the debt, or where the sheriff would not have confirmed the scheme if he had known of the omitted debt.

4.136 *"Subsequent" debts.* Notwithstanding the restrictions on a debtor obtaining credit which we propose could be included in schemes,[1] the debtor might incur a new debt subsequent to the confirmation of the scheme or indeed between the first notice date and confirmation. Under bankruptcy legislation, "subsequent" creditors cannot rank in sequestrations nor execute diligence after sequestration on pre-sequestration assets.[2] Under the Bankruptcy (Scotland) Act 1913, in certain circumstances a subsequent creditor could execute diligence on post-sequestration assets and rank in a second sequestration relating to those assets,[3] but under the Bankruptcy (Scotland) Bill 1984 post-sequestration assets and the income therefrom vest in the trustee,[4] and it appears that only income not payable to the trustee by court order may be attached by the diligence of post-sequestration creditors.[5] In England and Wales, a subsequent creditor may be scheduled to an administration order but will not be entitled to any dividend under the order until the pre-order creditors are paid to the extent provided by the order,[6] but the Cork Report recommended that a subsequent debt could not be included in their proposed debt arrangement orders, even as a deferred debt, except in limited circumstances.[7] The Australian Law Reform Commission on the other hand have recommended that a subsequent creditor if so advised should be entitled to apply for inclusion in a regular payments plan,[8] and we prefer that solution.

4.137 We propose therefore that a subsequent creditor should have the same options as other omitted creditors, i.e. he should be entitled to wait till after the scheme has terminated to enforce his debt or to apply for inclusion in, or revocation of, the scheme. We concede that in some cases this solution could be regarded by pre-scheme creditors as unfair and induce some to oppose scheme applications. However, if subsequent debts were incurred in breach of a restriction in the scheme on the debtor obtaining credit, a pre-scheme creditor would normally have a good case supporting an application by him for revocation of the scheme. Moreover, cases could arise where it would seem unjust to exclude a subsequent creditor, as where the subsequent creditor provided necessaries under credit arrangements not struck at by the credit restriction, and default occurred, all soon after the scheme's confirmation. A judicial discretion to include a subsequent debt, to revoke a scheme, or to retain the scheme as originally confirmed, takes account of the reality that circumstances could vary greatly.

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[1]See Recommendation 4.5 (para. 4.49).
[2]Bankruptcy (Scotland) Bill 1984, Sched. 1, para. 1(1); clause 36; Bankruptcy (Scotland) Act 1913, s. 117; ss. 103 and 104.
[3]*Grant* v. *Green's Tr.* (1901) 3 F. 1016.
[4]Bankruptcy (Scotland) Bill 1984, clause 31(1) and (5).
[5]Clause 31(2)–(4).
[6]County Courts Act 1984, s. 113(*d*).
[7]Para. 319.
[8]A.L.R.C. Report No. 6, para. 76.

(c) *Recommendations on late inclusion*

4.138 We **recommend:**

(1) Subject to the recommendation made below on "late" inclusion, there should be excluded from a debt arrangement scheme any debt which, at the first notice date, was:

(*a*) future or contingent;

(*b*) either (i) unconstituted by decree (or other document of debt) and disputed as to liability or quantum or (ii) constituted but disputed as to the amount remaining unpaid;

(*c*) due under a credit agreement subject to an application under the Consumer Credit Act 1974, section 139 (re-opening of extortionate credit agreements).

(2) (*a*) An application by the debtor under the 1974 Act, section 139 should not be competent after the first notice date in a scheme application and thereafter while the scheme application was pending or the scheme was in force.

(*b*) The sheriff's powers under the 1974 Act, section 139 to reopen extortionate credit agreements should not be exercisable in a scheme application but only in other proceedings (if commenced before the first notice date).

(3) (*a*) As a general rule, the administrator should include in a draft scheme:

(i) any debt identified after the first notice date and while the scheme application was pending;

(ii) any debt newly incurred since the first notice date which was undisputed as to liability or quantum and otherwise eligible under the above rules; and

(iii) any debt ineligible for inclusion by reason of being future, contingent, disputed or subject to challenge under the 1974 Act, section 139 at the first notice date if that reason ceased to obtain while the scheme application was pending.

(*b*) The administrator should not, however, include the debt where:

(i) the sheriff took the view that, having regard to the stage which the scheme application had reached, a later application by the debtor for variation of the scheme after its confirmation would be a more appropriate way of dealing with the question of inclusion; or

(ii) the inclusion of the debt would have the effect that the total included debts would exceed to a substantial extent the upper limit on indebtedness recommended above.

(*c*) If the existence, and eligibility for inclusion, of the debt was ascertained by the administrator after copies of the draft scheme had been served on creditors, the scheme should be adjusted to include the debt, and re-served on creditors. A new period for objections should be allowed.

(4) The sheriff should have a discretionary power, on application by a creditor and after giving interested persons an opportunity to make representations, to vary a confirmed scheme so as to include a debt which:

(*a*) had been omitted from the scheme in error;

(*b*) had been incurred since the first notice date and was undisputed; or

(*c*) had been excluded from the scheme as future, contingent, disputed or subject to an application under the 1974 Act section 139 as at the first notice date but had subsequently become eligible for inclusion as presently payable and no longer disputed nor subject to such an application.

But there should be no such inclusion if the effect would be that the total included debts would exceed to a substantial extent the upper limit on indebtedness recommended above.

(5) A creditor omitted from a scheme should have the options of making an application to the sheriff for inclusion of his debt by variation of the scheme, or for revocation of the scheme, or a combined application in the alternative for variation or revocation, or of staying outside the scheme and enforcing his debt in full on termination of the scheme notwithstanding any composition in the scheme of the other debts. (Recommendation 4.16; clauses 15(1), (3) and (5)(*c*), 23(1), (2), (4) and (5), 28(1) and (3) and 30; Schedule 7, paragraph 22.)

(d) *Ascertaining amount for ranking of debts identified, incurred or becoming eligible for inclusion only after first notice date: decrees for undischarged debts*

4.139 We proposed above[1] that for the purpose of ranking creditors on the product of a scheme, and on each disbursement by the administrator under a scheme, the amount of a debt payable and otherwise eligible for inclusion at the first notice date should be fixed by reference to the amount due as at that date. This rule would require modification in the case of certain debts which were identified by the administrator, or were incurred, or became eligible for inclusion, either (1) between the first notice date and confirmation of the scheme or (2) during the currency of the scheme.

4.140 It will be seen that the first of these categories comprises debts included in the scheme as confirmed, which were (*a*) payable and otherwise eligible for inclusion at the first notice date but only identified by the administrator thereafter; or (*b*) ineligible at the first notice date but became eligible for inclusion thereafter because the circumstances requiring exclusion no longer obtained; or (*c*) incurred after the first notice date. It would scarcely be possible to prescribe by statute a single date applicable to all these types of debt, such as the first notice date (which would not be apt for a future, contingent or disputed debt) or the date when the debt became payable (which would not be apt for a disputed debt, especially if court expenses were awarded against the debtor later, or a debt subject to an application under the Consumer Credit Act 1974, section 139). To prescribe a different date for different types

[1]Recommendation 4.10 (para. 4.80).

of debt would be unduly complicated since *inter alia* a debt may be ineligible on more than one ground (e.g. a debt may be contingent, disputed and subject to an application under the 1974 Act, section 139). In these circumstances, we propose a simple, flexible rule. The amount of the debt should be fixed by reference to the date when the administrator became satisfied as to the eligibility and the amount of the debt. If a draft scheme had already been circulated to creditors, we have proposed that the scheme would be adjusted to include the debt and re-circulated, and the date would be specified in the adjusted scheme: if a draft of the scheme had not yet been circulated, the date would be specified in the original draft scheme.

4.141 The second category of debts are those included by the sheriff in an order varying a confirmed scheme. We propose for those debts a simple rule that the amount of the debt should be fixed by reference to the date when the application for variation of the scheme was lodged. The sheriff would have a discretion to include or exclude the debt, and could delay inclusion until, for example, the expenses of a court action had been agreed or extracted. To prevent a creditor included late from obtaining a disproportionately large share of subsequent disbursements under the scheme, the creditors included in the scheme as originally confirmed would continue to rank on future disbursements along with the late creditor rateably in proportion to the amount of their debts as originally included in the scheme, and not as at the date of variation. This solution seems preferable to other options such as payment to the "late" creditor of a balancing disbursement, or deferment of his claim till the original debts were paid, which seem to us to favour unduly the late creditor and the original creditors respectively. Where there were two variation orders including creditors "late" at different times, the first of these creditors would continue to rank for his debt as it stood at the time of the first application for variation while the second would rank for his debt as it stood at the time of the second application for variation.

4.142 A creditor included "late" by variation of a confirmed scheme would receive a smaller number of disbursements under the scheme than creditors included from the beginning. The unpaid balance of the debt should therefore be excepted from the discharge of the debts which would be granted at the end of a successful scheme. We propose, however, that at the same time as the sheriff granted such a discharge, he would be under a duty to grant a special kind of decree in favour of the "late" creditor which would (*a*) contain a time to pay direction providing for payment of the unpaid balance of the sum due to the creditor under the scheme (i.e. in a composition scheme, the unpaid balance of the creditor's dividend and including any interest claimed in a scheme providing for payment in full) and (*b*) provide that if the time to pay direction lapsed through the debtor's default, the unpaid balance of the whole debt (not the unpaid balance of the composition) would become payable. In this way, "late" creditors included in a scheme after its confirmation would be treated in much the same way as creditors included from the beginning. A decree of the kind just described should be competent though the debt had been previously constituted by decree, and any previous decree would become inoperative when the new time to pay decree took effect. The time to pay direction should be capable of variation by the sheriff, but not

recall since, if there had been a composition, recall would deprive the debtor of the benefit of the composition.

4.143 We **recommend:**

(1) Where the administrator included in a draft scheme a debt which was:

(*a*) payable and otherwise eligible for inclusion at the first notice date but only identified by the administrator thereafter; or

(*b*) incurred after the first notice date; or

(*c*) ineligible for inclusion at the first notice date (as being future, contingent, disputed, etc.) but became eligible for inclusion thereafter,

the amount of the debt should be fixed by reference to the date when the administrator became satisfied as to the eligibility of the debt for inclusion and as to its amount, including court and diligence expenses incurred to that date for which the debtor was liable. That date should be specified in the draft scheme originally served on creditors or, if the debt was included after such service, in the scheme as adjusted and re-served on creditors.

(2) (*a*) Where the sheriff included a debt by variation of a confirmed scheme, the amount of the debt should be fixed by reference to the date when the application was lodged.

(*b*) Creditors previously included in a scheme would continue to rank on future disbursements rateably in proportion to the amount of their debts as fixed by reference to the first notice date or other date fixed for ascertaining the amount of their debt under the above proposals.

(3) A debt included "late" after confirmation of a scheme should be excepted from the discharge of debts on termination of a successful scheme. But at the time of granting the discharge of other debts the sheriff should be required to grant a decree decerning (*a*) for payment of the unpaid balance of the sum due to the creditor under the scheme (being in a composition scheme the unpaid balance of the dividend, and including interest claimed in a scheme providing for payment in full) together with a time to pay direction for payment of that balance by instalments or deferred lump sum, and (*b*) if the time to pay direction ceases to have effect by reason of the debtor's default or death, for payment of the unpaid balance of the whole debt (not the unpaid balance of the dividend in a composition scheme). The time to pay direction should be subject to variation, but not recall, by the sheriff's order.

(Recommendation 4.17; clauses 16(2) and 31(1), (6)–(8) and (10).)

(e) *Stoppage of diligence enforcing omitted debts and safeguards for creditors executing diligence*

4.144 *Stoppage of diligence enforcing omitted debts.* An interim order sisting diligence pending disposal of a scheme application would only bind creditors on whom a copy of the order had been served and accordingly would not affect diligence executed by a creditor in ignorance of the scheme application.

4.145 We considered whether a scheme should only preclude and render ineffectual diligences by included creditors or at least creditors to whom the confirmation of the scheme had been intimated. In the case of a creditor wrongly omitted from a scheme, the debtor would only have himself to blame for not disclosing the debt. We think, however, that fairness to creditors included in a scheme requires that all diligence by any creditor, included or not, should be incompetent while the scheme was in operation. This approach is consistent with the position in sequestrations under bankruptcy legislation where the interest of the sequestration creditors in the bankrupt's property is protected against the diligences of individual creditors, including post-sequestration creditors, even if the diligence is executed without actual notice of the sequestration.

4.146 *Safeguards for creditors executing diligence.* As a consequence of the stoppage of diligence, executed before or during a scheme, certain safeguards for creditors would be necessary. *First*, we propose that it should be expressly provided by statute that a creditor should not be liable in damages to the debtor by reason only of commencing or executing any diligence rendered incompetent by a debt arrangement scheme unless the debtor proved that at the time of executing the diligence the creditor was aware that the scheme had been confirmed. *Second*, legislation should also expressly provide that registration of a scheme (in accordance with proposals made below) should not be treated as fixing a creditor with constructive knowledge or awareness that a scheme is in force. In a reparation action by the debtor for wrongful diligence, the debtor should be required to establish that the creditor had actual knowledge of the scheme. Registers of schemes should be a facility to be used by creditors if so advised: and the many thousands of creditors executing diligence every year should not be required to search the register to avoid liability for wrongful diligence. *Third*, a creditor executing diligence while unaware of a scheme should, if he stays out of the scheme, nevertheless be entitled, after the termination of the scheme (whether on revocation or discharge of debts in a successful scheme), to recover the expenses of the diligence chargeable against the debtor so far as incurred before he became aware of the scheme. For this purpose, the rule recommended below[1] that in general the expenses of a diligence of certain types (poinding and sale, earnings arrestment, and conjoined arrestment order) should be recoverable only by that diligence should not apply. If the creditor were included in the scheme by variation order, he should be entitled to rank for those expenses in the scheme. *Fourth*, a creditor whose prior competently executed diligence was rendered ineffectual by the confirmation of a scheme should be entitled to recover the expenses of his diligence (so far as chargeable against the debtor) after the termination of the scheme, and again the proposed new general rule restricting the recovery of diligence expenses should not apply. *Fifth*, where a debt had not been discharged by a scheme and became enforceable by diligence on the termination of the scheme, and a poinding enforcing the debt had been either competently executed before the scheme and rendered ineffectual by it or executed after confirmation of the scheme by a creditor unaware of the existence of the scheme, then the rule proposed

[1]Para. 9.58; Recommendation 9.9(1).

below[1] prohibiting second poindings on the same premises for the same debt should not apply.

4.147 Notwithstanding our proposed rule that the expenses of a diligence of certain types[2] should in general be recoverable only by that diligence and not by any other legal process, the expenses of such a diligence should be eligible for inclusion in a scheme unless the creditor was entitled to complete his diligence despite the scheme. Thus, diligence expenses incurred prior to the first notice date would be included as mentioned above. Moreover, where a creditor had competently executed diligence after the first notice date, and the diligence was then rendered ineffectual by confirmation of the scheme, the creditor should be entitled to apply for a variation order including those expenses in the scheme as a "subsequent" debt so far as the expenses were chargeable against the debtor. On the other hand, a creditor whose arrestment or poinding had proceeded to the stage of warrant of sale or decree of furthcoming before the creditor received intimation of the interim order could, under our proposals, competently complete his diligence notwithstanding confirmation of the scheme: having regard to that fact, we think that such a creditor should take his chance of recovering expenses from the proceeds of his diligence and that any expenses not so recovered should not be eligible for inclusion in the scheme.

4.148 We **recommend:**

(1) The recommendation[3] that a debt arrangement scheme should render existing diligences ineffectual and render incompetent diligences executed while a scheme was in force should apply to diligences at the instance of omitted creditors as well as included creditors.

(2) The following safeguards for creditors executing diligence while a scheme was in force should be enacted.

(*a*) A creditor should not be liable in damages for executing diligence rendered incompetent by a scheme unless at the time of execution he had been aware that the scheme was in force.

(*b*) The registration of a scheme recommended below[4] should not be treated as constructive notice to a creditor of a scheme.

(*c*) A creditor executing diligence while unaware of a scheme should be entitled, after termination of the scheme, to enforce recovery in full of the diligence expenses chargeable against the debtor notwithstanding Recommendation 9.9(1) at para. 9.58 for restricting the recovery of such expenses.

(3) The restriction on second poindings in the same premises recommended in Chapter 5[5] should not apply to poindings enforcing debts undischarged on termination of a scheme if the previous poinding had been either executed before confirmation of the scheme and rendered ineffectual

[1]Para. 5.134; Recommendation 5.28(1).

[2]A poinding and sale, an earnings arrestment, and a conjoined arrestment order: see Recommendation 9.9(1) (para. 9.58).

[3]Recommendation 4.14 (para. 4.118).

[4]Recommendation 4.38 (para. 4.267).

[5]Recommendation 5.28(1) (para. 5.134).

by it or had been executed after confirmation when the creditor was unaware that the scheme subsisted.

(4) It should be competent to include diligence expenses chargeable against the debtor in a debt arrangement scheme (notwithstanding Recommendation 9.9(1) at paragraph 9.58 restricting the recovery of those expenses), unless the creditor was entitled to complete his diligence despite the scheme.
(Recommendation 4.18; clauses 18(1)–(4), (6), 38(2), 118(4)(*b*) and (5).)

(5) Sums paid to creditor or recovered by diligence outside a scheme

4.149 We have proposed that partial payments to account of debts after the first notice date (or other date prescribed for ascertaining the amount of a debt) should not be taken into account for the purposes of a debt arrangement scheme in order to promote equality between creditors and to minimise the need for adjustment or variation of schemes. Most debtors would be unlikely to make payments to a creditor outside a scheme after the first notice date. Such payments, moreover, could give an unfair preference to a creditor which, if brought to the sheriff's notice, would justify the refusal of a scheme application or the revocation of a scheme. It is possible, however, that the debtor might feel constrained to make payments to account of, for example, past rent arrears or fuel debts included in a scheme, to prevent ejection from his residence or discontinuance of gas or electricity supplies. A relative or friend might pay a debt voluntarily, or a co-obligant bound along with the debtor might do so under legal obligation.

4.150 We propose that where a creditor whose debt was included in a draft scheme or a scheme received payment of the amount to which he was entitled under the scheme, wholly from payments outside the scheme, or partly from such payments and partly from disbursements under the scheme, he should be required to intimate this fact to the administrator as soon as reasonably practicable. Payments by a co-obligant outside the scheme, however, would fall to be be ignored unless and until the unpaid balance of the whole debt (not the composition in a composition scheme) was satisfied. The reason is that a creditor is entitled to receive his composition in a scheme and the deficit from a co-obligant. (We revert later[1] to the rule allowing subrogation of a co-obligant on payment of the whole debt (not the composition) or that part of the whole debt for which he is liable.)

4.151 The administrator should have an express statutory title to recover from the creditor (*a*) payments made by the administrator after the creditor had received the amount due to him under the scheme, together with (*b*) interest at the rate applicable to sheriff court extract decrees.[2] The sheriff should be empowered to make an order decerning for payment to the administrator which would be enforceable by diligence. The expenses of any such diligence, if not met out of its proceeds, would be met out of the sums paid by the debtor to the administrator in priority to the creditors' claims, which failing by the public purse. We would expect, however, that the threat

[1]Para. 4.186.
[2]Sheriff Courts (Scotland) Extracts Act 1892, s. 9.

of diligence would normally suffice to elicit payment. We believe it would be useful if the sheriff had power to make an order requiring a creditor to give information to the administrator as to any payments made to the creditor outside the scheme. Breach of the order would be a contempt of court.

4.152 Where a debt had been paid outside a scheme, the level of the debtor's payments to the administrator ("in-payments") should not be reduced to reflect the debtor's reduced indebtedness. Those in-payments would have been set at a level which the court thought reasonable having regard to the debtor's income and other resources. The fact that a debt had been paid outside a scheme, whether by a relative or friend gratuitiously or by a co-obligant under legal obligation, should not affect the level of in-payments or the overall amount payable to creditors. The early discharge of a debt should simply lead to an increase in the rate of disbursements to other creditors under the scheme and to the earlier termination of the scheme. Accordingly, we propose that if the administrator ascertained the fact of payment of a debt between service to creditors and confirmation of a draft scheme, he would exclude the debt from the scheme, make any other necessary adjustments, and re-serve the adjusted scheme together with a notice allowing a new period for objections. If the administrator ascertained the fact of payment of the amount due to the creditor under the scheme after the scheme had been confirmed, he should cease making disbursements to the creditor and the sheriff, on the administrator's application, should vary the scheme by excluding the creditor's debt, increasing the amounts to be paid in disbursements under the scheme to the remaining creditors, and requiring disbursement to creditors under the scheme of any over-payments recovered from the creditor. This would be an automatic administrative procedure which would be simpler than an application to the sheriff for a discretionary order varying a scheme. Where, however, the administrator ascertained the fact of full payment of the sum due to the creditor under the scheme otherwise than by intimation by a creditor as mentioned at paragraph 4.150 above, the sheriff should not vary the scheme unless, after giving the creditor an opportunity to be heard, he was satisfied that full payment of that sum had indeed been made. In a case where a co-obligant had paid the full debt (not the composition) or the part thereof for which he was liable, we recommend later[1] that he should have 14 days within which he could claim to be subrogated for the original creditor in the scheme. If, however, the scheme had been varied so as to distribute the original creditor's share among the remaining creditors, there would be no share left to which the co-obligant could be subrogated (unless the scheme was again varied). We propose therefore that there should be a delay in varying the scheme of 14 days after the date when the administrator received intimation, or was otherwise satisfied, of payment of the debt. This should suffice to protect the co-obligant's right to claim subrogation.

4.153 We **recommend:**

(1) The sheriff should have power to make an order requiring a creditor to give information to the administrator as to payments received by him outside the scheme.

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[1]Recommendation 4.27(6) (para. 4.193).

(2) Where a creditor whose debt was included in a scheme or draft scheme received payment of the full amount due to him under the scheme, whether wholly from payments outside the scheme or partly from such payments and partly from payments under the scheme, he should as a general rule intimate that fact to the administrator as soon as practicable. As an exception to the general rule, payments by a co-obligant would be disregarded for this purpose unless payment by the co-obligant satisfied the unpaid balance of the whole debt (not the composition in a composition scheme).

(3) The sheriff should be empowered to order repayment to the administrator of sums paid by the administrator after the creditor had received the total amount due to him with interest at the statutory rate for sheriff court decrees. The order should be enforceable by diligence. The sheriff should also have power to order the creditor to inform the administrator of the amount of any over-payment.

(4) The early discharge of an included debt wholly or partly by payments outside the scheme should result in an increase in the rate of disbursements to creditors under the scheme.

(5) A procedure should be prescribed enabling the administrator to adjust a draft scheme to exclude a debt which was satisfied before confirmation of a scheme and to re-serve the adjusted scheme. A procedure should also be prescribed requiring the administrator to cease payments when the debt (or composition) was satisfied during the currency of the scheme and requiring the sheriff to vary the scheme by excluding the debt and increasing the disbursements to the other creditors. Where the creditor did not himself intimate satisfaction of the debt, the sheriff should give him an opportunity to be heard before excluding the debt.

(6) After the administrator receives intimation from the creditor or is otherwise satisfied of payment of a debt outside a scheme, there should be a short delay (of 14 days) before the scheme is varied under the foregoing procedure, to give time for a co-obligant to claim subrogation to the original creditor's debt as proposed in Recommendation 4.27 (paragraph 4.193) below.
(Recommendation 4.19; clause 33.)

4.154 In order to secure equality as between the creditors included in a confirmed scheme, we considered whether any poinding or arresting creditor whose diligence was completed by sale or furthcoming after the first notice date should be bound to pay the proceeds of the diligence (less diligence expenses incurred since the first notice date[1]), to the administrator. In the case of an earnings arrestment or conjoined arrestment order continuing after the first notice date, we considered whether sums recovered by creditors under those diligences since the first notice date should also be payable to the administrator by the creditor on confirmation of the scheme, or alternatively whether the sheriff should make an order requiring the employer to pay the sums to the administrator pending disposal of the scheme application. We have however rejected these options because of the legislative and adminis-

[1]The creditor would already have ranked for diligence expenses incurred prior to the first notice date so far as chargeable against the debtor.

trative complications which they would involve. It seems to us that the best solution would be to treat the net proceeds of diligences competently executed after the first notice date in the same way as, under the foregoing recommendation, payments to account of a debt made outside the scheme would be treated.

4.155 We **recommend:**

Sums recovered by diligence after the first notice date should be treated in the same way as payments to account of a debt would be treated in terms of Recommendation 4.19 above.
(Recommendation 4.20; clause 33.)

(6) Criminal fines etc., certain Crown debts and maintenance

(a) *Exclusion and enforceability of fines and other debts due under criminal court orders, and certain civil fines and penalties due to the Crown*

4.156 Following precedents in other legal systems, we consider that priority should in effect be given to criminal fines by excluding these debts from debt arrangement schemes, and by permitting their enforcement notwithstanding the stoppage of other diligences, even in cases where the criminal court has ordered the recovery of the fine by civil diligence[1] (which is at present very rare indeed in relation to offenders who are natural persons rather than bodies corporate). The court may itself order payment of the fine by instalments[2] and may change its order from a fine to a sentence of imprisonment in default of payment.[3] Such orders raise questions of sentencing policy in which the debtor's ability to pay (perhaps the central question in debt arrangement schemes) is only one factor. Further, to concede co-ordinate jurisdiction to the civil and criminal courts would create a confusing and troublesome overlap of powers.

4.157 Criminal fines already have a special status in insolvency law: thus in a sequestrian fines or other penalties due to the Crown and liabilities to forfeiture of bail are not discharged by the bankrupt's discharge.[4] The effect of exclusion of criminal fines from a debt arrangement scheme would be that the debtor would have to pay his criminal fines before meeting his civil liabilities under the scheme. It must just be accepted that default in payment of such a fine might result in the debtor's imprisonment with the result that the debtor could no longer earn wages or salary to make payments to creditors. Accordingly, the debtor should specify any liability for a fine in his statement of affairs and the administrator and the sheriff, in considering whether a debt arrangement scheme would have a reasonable prospect of success, should allow for the payment of any existing criminal fine by the debtor outside the scheme. If it were thought that insufficient surplus income would remain after payment of a fine then the application should be refused.

4.158 We prefer this approach to the alternative approach of including fines

[1]Criminal Procedure (Scotland) Act 1975, s. 411.
[2]*Ibid.*, s. 399(1).
[3]*Ibid.*, s. 407(1).
[4]Bankruptcy (Scotland) Bill 1984, clause 52(1) and (2)(*a*) and (*b*), replacing Bankruptcy (Scotland) Act 1913, s. 147.

in debt arrangement schemes as prior debts,[1] and we consider that our recommended approach should be adopted in relation to other liabilities arising out of criminal proceedings such as bail, caution or security due under an order of a court in criminal proceedings.[2] On consultation, it was represented to us that sums due under a compensation order against a convicted person made by a court in criminal proceedings[3] should be included in a debt arrangement scheme upon the view that the order is made in respect of what would otherwise be a civil debt. Debts under such compensation orders, however, may be varied by the criminal court and made payable by instalments; collection under the orders is undertaken by the clerks of court in like manner as collection of fines; and as in the case of fines imprisonment can be imposed in default of payment. Thus, in many respects sums due under compensation orders have more in common with fines than they have with civil debts. We conclude therefore that compensation orders in criminal proceedings should be treated in the same way as criminal fines orders and excluded from debt arrangement schemes.

4.159 Because of their quasi-criminal character, the same policy should apply to fines or penalties due to the Crown imposed for contempt of court in civil proceedings, or for professional misconduct under particular enactments regulating professions, or under section 91 of the Court of Session Act 1868. We understand that civil penalties imposed for failure to pay tax are generally recovered by the Revenue Departments along with the taxes to which they relate and on balance we think that they should not be excluded from debt arrangement schemes.

4.160 We **recommend:**

(1) Priority should in effect be given to criminal fines by excluding them from debt arrangement schemes and by permitting their enforcement by imprisonment, or civil diligence under a warrant of the criminal court, while a scheme is in force.

(2) The same rule should apply to other debts (such as bail, caution, security or compensation) due under an order of a court in criminal proceedings, and fines or penalties imposed for contempt of court in civil proceedings.
(Recommendation 4.21; clause 42(1), definition of "debt", as read with clause 4(7).)

(b) *Aliment, periodical allowance and analogous maintenance obligations*

4.161 Aliment and periodical allowance on divorce due by the debtor raise a number of problems. In a sequestration whether under the existing law or under the Bankruptcy (Scotland) Bill 1984, an alimentary creditor of the bankrupt will rank as an ordinary creditor in respect of arrears of aliment due

[1]In England and Wales criminal fines may be included as prior debts in attachment of earnings orders under the Attachment of Earnings Act 1971 but there appears to be no *express* exclusion of fines from administration orders. Criminal fines are excluded from arrangements or plans under the Australian and Canadian federal legislative proposals.

[2]E.g. Criminal Procedure (Scotland) Act 1975, ss. 190, 284, 289, 391, 445; Bail etc. (Scotland) Act 1980, s. 1(3).

[3]Criminal Justice (Scotland) Act 1980, Part IV.

under a court decree or agreement at the time of sequestration, but cannot rank as a contingent creditor for future aliment accruing during the sequestration.[1] The principle underlying the present law is that the latter claim is inconsistent with the nature of aliment; which is due only when the alimentary debtor has a surplus. There can be no surplus if he is insolvent: so a maintenance creditor must follow the maintenance debtor's fortunes.[2] Where, however, the court makes an order under bankruptcy legislation for the payment of instalments to the trustee in the sequestration out of the bankrupt's income,[3] the court will allow the debtor to retain part of his income not only for his own subsistence but also for the support of his alimentary dependants, at least if living in family with him.[4]

4.162 The effect of these rules is that a maintenance creditor to whom pecuniary maintenance is owed does not compete with ordinary creditors in the distribution of the bankrupt's assets (except in respect of a claim for maintenance arrears), but a maintenance creditor may be supported by him out of current (after-acquired) personal earnings and other income, at least if living in family with him. The practical justification for the latter rule is that, whereas it is possible to divest a bankrupt of his assets compulsorily in order to distribute them to his creditors, it is not possible to compel him to work for his creditors without allowing him to retain enough for the subsistence of himself and his immediate family. We think, however, that different considerations apply where the maintenance creditors are a separated or former spouse, or children, living apart from the debtor. First, where the debtor is maintaining persons as dependants in his household, there is as it were a common roof, hearth and table which would generally make it inhumane and impracticable to make support available to the debtor but not the other members of the household. Second, the debtor is likely to want to support the dependants whom he is maintaining in his household: if not allowed to do so, he is likely to give up his paid employment, so that a scheme would not be feasible. Third, for the purpose of supplementary benefit, regard will be had to the debtor's household: the spouse and children who are living with the debtor will not be able to claim supplementary benefit. In all these respects, the position of separated maintenance creditors is, or is likely to be, different, though there will be cases where the debtor wishes to support maintenance creditors, especially children, to whom he owes pecuniary aliment.

4.163 We propose that there should not be rigid rules defining the liabilities (whether for maintenance or anything else) which a debtor can meet out of income before fulfilling his obligations under the scheme. We propose that a scheme should be competent only if the debtor's resources would suffice to yield a minimum sum over three years after meeting the daily needs of himself and any person whom he is maintaining in his household.[5] In the light

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[1] *Matthews* v. *Matthews' Tr.* (1907) 15 S.L.T. 326; *Barnes* v. *Tosh* (1913) 20 Sh. Ct. Reps. 340: Bankruptcy (Scotland) Bill 1984, Sched. 1, para. 2.

[2] *Reid* v. *Moir* (1866) 4 M. 1060, 1063.

[3] Bankruptcy (Scotland) Bill 1984, clause 31(2) replacing the vesting declarator relating to income under the Bankruptcy (Scotland) Act 1913, s. 98(1), *Caldwell* v. *Hamilton* 1919 S.C. (H.L.) 100.

[4] See *Birrell's Tr.* v. *Birrell* 1957 S.L.T. (Sh. Ct.) 6.

[5] Recommendation 4.9(5) (para. 4.72); see clause 17(4) of the Bill annexed to this report.

of that provision, we would expect that, in assessing whether a scheme was feasible, the administrator and sheriff would take into account the debtor's obligations to aliment such dependants, but generally not dependants living in a separate household and that this would be reflected in the level of deductions from earnings fixed by any pay deduction order made in connection with the scheme.

4.164 We propose that a maintenance creditor to whom periodical allowance on divorce or pecuniary aliment is owed should rank in a debt arrangement scheme for arrears accrued up to the first notice date. To that extent, maintenance arrears should be treated like any other ordinary debt. It should not, however, be competent to include maintenance payments falling due after the first notice date whether in the scheme as originally confirmed or by way of an application to the sheriff for late inclusion of those payments after confirmation of the scheme.

4.165 As regards existing diligences by maintenance creditors, any current maintenance arrestment, and any conjoined arrestment order under which maintenance was payable,[1] operating against the debtor's earnings while the scheme application was pending would continue unaffected by the interim order sisting diligence, and that order would not render incompetent the execution of a new current maintenance arrestment while the scheme application was pending. Since the maintenance debtor would by that stage be insolvent, in principle current maintenance ought no longer to be due:[2] the maintenance debtor's remedy would be an application for recall of the award of periodical allowance or aliment to the court which had made that award. If this consequence seems harsh especially as regards children entitled to pecuniary aliment, it must be borne in mind that such children would be entitled to receive supplementary benefit which is usually a more regular and secure source of income than pecuniary aliment.[3] Though aliment may be due at a higher level where the alimentary debtor's "station in life" is above that of supplementary benefit, we do not think that this consideration should be given any weight. A scheme debtor cannot be allowed to pay pecuniary aliment for, say, boarding school fees while he is in debt to his ordinary creditors. It seems better that, while a scheme is in force, the separated family should be supported by the State through supplementary benefit than by the debtor at the expense of his creditors. And where supplementary benefit has been provided to the maintenance creditor, the D.H.S.S. may in certain cases recover the cost from the maintenance debtor:[4] where the maintenance debtor is insolvent, it seems unfair to prefer the D.H.S.S. to his ordinary creditors.

4.166 The recall of a maintenance decree would have the effect, after intimation, of terminating the current maintenance arrestment or as the case

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[1]See Chapter 6 for a description of these diligences.

[2]*Reid* v. *Moir* (1866) 4 M. 1060. Under the Family Law (Scotland) Bill 1984, clauses 4(1) (aliment) and 8(2)(*b*) (periodical allowance on divorce) the court is bound to have regard to the resources of the parties, and resources must mean resources remaining after meeting ordinary debts due by the maintenance debtor to other creditors.

[3]The rates of aliment and supplementary benefit are compared in Doig, *The Nature and Scale of Aliment and Financial Provision on Divorce in Scotland* (1982), Scottish Office Central Research Unit Papers, para. 6.17.

[4]Supplementary Benefits Act 1976, ss. 18 and 19.

may be payment of maintenance from earnings under the conjoined arrestment order. As indicated above, the interim order should prevent, pending disposal of the scheme application, the grant of warrant for imprisonment of the debtor for wilful default under the Civil Imprisonment (Scotland) Act 1882, section 4, since imprisonment would prejudice the success of a scheme application or a scheme. If the debtor were truly insolvent, it is unlikely that such an application would be successful.

4.167 The commencement of the scheme would render ineffectual all diligences against the debtor's earnings, including earnings arrestments recovering arrears of maintenance, current maintenance arrestments recovering maintenance as it falls due, and conjoined arrestment orders recovering maintenance whether arrears or current. Similar considerations apply to periodic payments due under non-Scottish maintenance orders and agreements enforceable in Scotland and under contribution orders in respect of children in care and orders or decrees against liable relatives for the recovery of the cost of supplementary benefit, which we propose should be treated in the same way as periodical allowance and pecuniary aliment under Scottish decrees and agreements.

4.168 We **recommend:**

(1) A maintenance creditor to whom maintenance (periodical allowance on divorce or pecuniary aliment) is owed should rank for arrears accrued up to the first notice date, but not for maintenance payable after that date.

(2) An interim order sisting diligence should not preclude or affect a current maintenance arrestment, or a conjoined arrestment order enforcing current maintenance, such as we recommend in Chapter 6.

(3) The confirmation of a scheme should render incompetent and ineffectual new and existing current maintenance arrestments and conjoined arrestment orders enforcing current maintenance.

(4) Diligences enforcing arrears of maintenance should be affected by an interim order and the coming into force of a scheme in the same way as diligences enforcing ordinary debts would be so affected (as recommended above[1]).

(5) An interim order sisting diligence and the coming into force of a scheme should render incompetent an application for and the grant of a warrant for civil imprisonment of the debtor for failure to pay aliment.

(6) The above rules should apply to maintenance agreements registered for execution, decrees and contribution orders for periodical sums enforcing recovery of supplementary benefit or the cost of maintaining children in care, and analogous non-Scottish judgments and instruments enforceable in Scotland.
(Recommendation 4.22; clauses 15(1), 18(1) and (4), 20(3), 23(3), 28(2), 42(1) (definition of "debt" and "decree") and 74 (definition of "maintenance" and "maintenance order").

[1]Recommendations 4.13 (para. 4.109) and 4.14 (para. 4.118).

(7) Debts secured or enforceable by remedies other than ordinary diligence

(a) *Debts secured by contractual securities*

4.169 *Heritable securities*. In Scots law, a heritable creditor's remedies under a standard security depend on whether the security has a non-default calling-up clause (which allows the security to be called up on one month's notice even in the absence of default[1]) or whether his remedies become available only on the debtor's default. In either case, however, the borrower's rights to delay enforcement proceedings are more limited than elsewhere in the United Kingdom.[2] Apart from cases of heritable securities securing regulated agreements under the Consumer Credit Act 1974, the courts in Scotland do not possess powers to restrain the calling up of a standard security over a dwelling-house or to delay enforcement proceedings to give time to pay.[3] As from the coming into operation of the relevant provisions of the Consumer Credit Act 1974 on 19 May 1985, enforcement of a standard security securing a regulated agreement usually requires, in addition to a notice of default or calling up notice under the general law on standard securities, a default notice under section 87 of the 1974 Act, and a court order authorising enforcement of the security under section 126 of the 1974 Act.[4] In our Consultative Memorandum No. 50 we invited comments on whether, in the case of a loan heritably secured over the debtor's home, the sheriff in a debt arrangement scheme should have power to suspend, for the duration of the debt arrangement scheme, the personal obligation to repay capital instalments, the amount not paid being made up on the termination of the scheme.[5] There was no dissent from our provisional view that restraints on the calling-up of standard securities could only be appropriately considered in a review of heritable securities over the homes of all debtors, not merely those fortunate enough to obtain debt arrangement schemes. We adhere to that view.

4.170 In many debt arrangement scheme cases, such a restraint would be neither practicable nor reasonable. If the debtor had "mortgaged" his house completely (e.g. by a second or subsequent heritable security), he could scarcely expect to keep it. On the other hand, if the debtor had a considerable reversionary interest in the house, the cases would be rare where he could reasonably offer his creditors merely a composition, or even obtain time to pay his debts in full, especially if he was meantime building up an asset of considerable value by capital payments. We do not, however, think that the mere existence of a heritable security should be an absolute bar to a debt arrangement scheme;[6] there may be cases where the heritable creditor and other creditors accept the debtor's proposals for payment and agree to allow

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[1]Conveyancing and Feudal Reform (Scotland) Act 1970, s. 19, Sched. 3, para. 8.

[2]The loan agreement will normally stipulate that on default, the whole unpaid balance of the principal sum, together with interest accrued, will become immediately payable. On default the heritable creditor can proceed to sell on one month's notice without judicial warrant: 1970 Act, Sched. 3, para. 10. He can raise an action of ejection immediately on default (1970 Act, s. 24) and the court has no discretion to refuse or delay warrant of ejection: *United Dominions Trust Ltd.* v. *Site Preparations Ltd. (No. 1)* 1978 S.L.T. (Sh.Ct.) 14.

[3]Compare Administration of Justice Act 1970, s. 36(1); Administration of Justice Act 1973, s. 8.

[4]See Wood, "The Consumer Credit Act 1974" (1985) 30 J.L.S.S. 130, 133.

[5]Proposition 18(2) (para. 2.55).

[6]We propose that a heritably secured loan should be excepted from the upper financial limit on the indebtedness of a debtor applying for a scheme.

him to keep the house, and other cases in which the scheme could come into operation while the heritable creditor called up his security. We think that if debt arrangement scheme procedure is to be a ground of calling-up a standard security, the security should expressly so provide and that such a consequence should not be a statutory standard condition of such a security.[1] Moreover, while we propose elsewhere[2] that references to "apparent insolvency" (or "notour bankruptcy") in irritant clauses in legal documents should in future be presumed to include a reference to an order appointing an administrator in a debt arrangement scheme, this presumption should not apply to references to apparent insolvency in heritable securities.

4.171 In our view, to enable a heritable creditor to value his security and rank for the balance in a debt arrangement scheme would be too complicated a solution. We propose therefore that a heritably secured debt should not be included in a debt arrangement scheme unless and until the heritable creditor had either discharged his security, or realised the security subjects, or acquired them by "foreclosure" in partial satisfaction of the debt. It should, however, be made clear that a scheme was competent which assumed that payments would be made outside the scheme to account of a debt heritably secured over the debtor's residence. Thus, we have proposed above[3] that a scheme application should be entertained only if it appeared to the sheriff that the debtor's resources left to him after meeting "daily needs" would be sufficient to yield a minimum sum for creditors: and we further propose that it should be made clear that "daily needs" for this purpose may include periodic payments required to be made by the debtor outside the scheme in respect of a security over his residence. Whether there was a need for such payments would also be an important factor taken into account by the sheriff in considering whether to confirm a scheme which assumed that such payments would be made. We also propose that the sheriff having jurisdiction over a debt arrangement scheme should be empowered to make an order requiring a heritable creditor who had exercised his power of sale under a heritable security to pay to the administrator the balance of the net proceeds of sale which would otherwise be payable to the debtor as owner of the subjects. The order should authorise enforcement by diligence of the sum payable as if it were a debt due to the administrator, and the expenses of the diligence, if not met by its proceeds, would be met by the fruits of the scheme in priority to creditors' claims, which failing by the public purse.

4.172 *Securities over moveables*. In the case of contractual securities over moveables (e.g. pledges and assignations of life assurance policies or shares[4]), the secured creditor should also have the option of realising the security subjects and ranking for the balance by applying for late inclusion or discharging the security and ranking in the scheme for the whole debt. It would be too complicated to allow the creditor to value his security and rank for the deficiency.

4.173 *Interest*. Where a contractual security secured payment of interest on

[1]See Conveyancing and Feudal Reform (Scotland) Act 1970, Sched. 3, para. 9.
[2]Recommendation 4.46(1) (para. 4.311).
[3]See para. 4.70.
[4]We deal later with securities created by operation of law, such as hypothecs and liens.

the debt, the creditor would be entitled to recover interest in full out of the proceeds of sale of the secured subjects notwithstanding the existence of a composition scheme. In ranking for the unsecured and unpaid balance of the principal sum and interest after realisation, however, the rules as to interest on unsecured debts outlined above would apply.

4.174 We **recommend:**

(1) An interim order sisting diligence and a debt arrangement scheme should not affect the entitlement of the creditor under a contractual security to exercise the rights and remedies by which his security is enforceable (such as rights of calling-up the security, entry into possession, ejection from heritage, realisation of the security subjects, and acquisition of the subjects by foreclosure in default of sale).

(2) A debt secured by a contractual security over heritable or moveable property of the debtor (as distinct from the property of a cautioner or other co-obligant) should be excluded from the scheme unless and until the creditor had discharged the security, or sold the security subjects under his power of sale, or acquired them in partial satisfaction of the debt.

(3) Provision should be made amending the Conveyancing and Feudal Reform (Scotland) Act 1970, Schedule 3, paragraph 9 (which makes it a standard condition in a standard security that the debtor shall be held in default when the proprietor of the security subjects has become insolvent) to make it clear that the proprietor should not be held insolvent for the purposes of that paragraph by reason only of the fact that a debt arrangement scheme has been applied for or confirmed.

(4) In determining whether the debtor's resources after meeting his "daily needs" would exceed the "minimum product threshold" for scheme applications recommended above, the sheriff should be empowered, but not required, to treat as "daily needs" payments by the debtor outside a scheme in respect of a security over his residence.

(5) The sheriff should be empowered to make an order requiring a heritable creditor who had exercised his power of sale to pay to the administrator the surplus proceeds of sale otherwise due to the debtor. The order should be enforceable by diligence.

(Recommendation 4.23; clauses 15(7)(*a*), 17(4)(*a*), 23(1)(*g*), 26(4), 28(1)(*g*), 37 and 41(1), Schedule 7, paragraph 15.)

(b) *Debts enforceable by sequestration under the landlord's or superior's hypothec or by poinding of the ground*

4.175 As explained above,[1] sequestration for rent under the landlord's hypothec, sequestration for feuduty under the superior's hypothec, and poinding of the ground are diligences whereby special kinds of security, created by operation of law rather than by contract, are enforced. In a sequestration, full effect is given to the landlord's hypothec,[2] and partial effect is given to a poinding of the ground by a secured creditor executed within 60

[1]See paras. 3.39 and 3.40.

[2]Bankruptcy (Scotland) Bill 1984, clause 48(6) replacing Bankruptcy (Scotland) Act 1913, s. 115.

days before, or on or after, the date of sequestration, limited to interest on the *debitum fundi* for the current half yearly term and for the previous year.[1] We propose to review these forms of diligence in due course with a view to possible reform or abolition, but meantime we think that they should be treated in debt arrangement schemes in the same way as securities created by contracts.

4.176 We **recommend:**

(1) An interim order sisting diligence and a debt arrangement scheme should not affect the right of a creditor to use the "security diligences" of poinding of the ground or sequestration under the landlord's or superior's hypothec.

(2) Any debt enforceable by poinding of the ground or sequestration under the hypothecs should be excluded from a scheme unless and until the creditor agrees not to use those remedies to enforce that debt.
(Recommendation 4.24; clauses 15(8), 18(8), 20(3) and (7), 23(1)(*g*), 28(1)(*g*) and 41(1).)

(c) *Debts secured by creditors' liens or rights of retention over goods or papers*

4.177 Our consultation revealed disagreement on what should be the effect of a debt arrangement scheme on creditors' rights of retention or lien over goods or papers.[2] Such rights enable a creditor in possession of goods or papers belonging to the debtor to retain possession until the debt is paid (e.g. a repairer's lien for the cost of his services; a solicitor's or accountant's lien over papers for his fees; or the unpaid seller's lien over the goods sold). Generally the creditor can only sell the goods if he obtains a warrant of the court[3] or, in the case of the unpaid seller's lien, gives the buyer notice of intention to re-sell.[4] In a sequestration, the creditor must surrender the articles subject to the lien but is given a preference for the debt secured by the lien.[5] In the case of liens over corporeal moveables, the true worth of the lien to the creditor is the sale value of the goods; in the case of a lien over papers, the true worth of the lien to the creditor consists in withholding the use of the papers from the debtor as an inducement to payment, since the papers are not marketable.[6] We think that in the case of a lien over moveable goods (other than papers), the solution should be similar to that proposed for a contractual security (such as a pledge): the creditor should not rank in the debt arrangement scheme unless and until either he had realised the goods (under the court's warrant where necessary) in partial satisfaction of the debt or the lien had otherwise ceased to have effect. In the case of a lien over title-deeds, accounts and other papers the creditor should rank in the debt arrangement scheme in the same way as an unsecured creditor but should be entitled to retain the papers during the currency of the scheme. On discharge of the debt at the termination of the scheme or, as the case may be, on

[1]Bankruptcy (Scotland) Bill 1984, clause 36(6) replacing Bankruptcy (Scotland) Act 1913, s. 114.

[2]Consultative Memorandum No. 50, Proposition 24(2) (para. 2.69).

[3]*Gibson and Stewart* v. *Brown & Co.* (1876) 3 R. 328; *Parker* v. *Brown & Co.* (1878) 5 R. 979.

[4]Sale of Goods Act 1979, s. 48(3).

[5]*Train and McIntyre* v. *Forbes* 1925 S.L.T. 286.

[6]*Parker* v. *Brown & Co.* (1878) 5 R. 979, 981.

payment of the sums due under a time to pay decree mentioned at Recommendation 4.17(3),[1] the lien should fly off, this being an exception to the general rule that a discharge should not affect security rights. In view of the peculiar character of liens over papers as a security not leading to sale, this special solution seems justifiable.

4.178 We **recommend:**

(1) Debts secured by liens or rights of retention over goods other than papers should be treated in the same way as debts secured by contractual securities under Recommendation 4.23(1) and (2) (paragraph 4.174) above.

(2) Debts secured by a lien over papers should be eligible for inclusion in a scheme in the same way as unsecured debts and the scheme should not affect the creditor's right to retain possession of the papers during the currency of the scheme. The lien should be discharged by a discharge of the debt at the end of a scheme or on payment of the sums due under a time to pay decree mentioned at Recommendation 4.17(3) (paragraph 4.143).

(Recommendation 4.25; clauses 15(7)(*b*), 23(1)(*g*), 28(1)(*g*) and 41(2).)

(d) *Debts enforceable by compensation (set off) or retention of money (balancing of accounts in bankruptcy)*

4.179 The general rules of compensation (set off) under the Compensation Act 1592 as developed by the common law should apply where a debtor who has applied for or obtained a debt arrangement scheme (a scheme debtor) owes a liquid debt to one of his creditors who simultaneously owes a liquid debt to the scheme debtor. Under these rules, the two debts would be "compensated" or set off to the extent to which they corresponded in amount (i.e. the lesser debt), the balance remaining being the debt due to, or by, the scheme debtor. The debts must generally be liquid in the sense of presently payable (not future or contingent) and ascertained or immediately ascertainable (not disputed or uncertain as to liability or amount).

4.180 Where one of the parties is bankrupt, liquid debts can only be set off if the other party acquired right to the debt, as original creditor or assignee, before notice of bankruptcy.[2] In technical language, there must be "concourse of credit and debit"[3] before such notice. One at least of the main policies underlying this rule is to prevent a bankrupt's debtor from buying debts due by the bankrupt at a low figure and setting them off at face value in a subsequent bankruptcy process to the prejudice of the general body of creditors.[4] In bankruptcy processes, where the bankrupt is divested of his estate, the date of divestiture is taken as implying notice of bankruptcy.[5] Where the bankrupt is not divested of his estate (as would be the case in a

[1]Para. 4.143.

[2]Bell, *Commentaries,* vol- ii, p. 123; Goudy, p. 554.

[3]That is to say, the parties must be debtor and creditor in the debts simultaneously and each party must be debtor in the same legal capacity (e.g. personal or as trustee) as he is creditor.

[4]Goudy, pp. 554–5; *Liquidators of Highland Engineering Ltd.* v. *Thomson* 1972 S.C. 87, 91; *Cauvin* v. *Robertson* (1783) Mor. 2581.

[5]Bell, *supra*; Goudy, p. 555.

debt arrangement scheme) but is merely in "apparent insolvency" (notour bankruptcy) or absolute insolvency, it seems that set off is only competent if the bankrupt's creditor acquired right to the debt before actual notice of the bankruptcy or insolvency and possibly in good faith without the purpose of achieving set off.[1] We think that the common law should regulate any question of set off of liquid debts involving a scheme debtor. We propose below that registration of a debt arrangement scheme should not imply constructive notice of the existence of such a scheme:[2] accordingly it would not imply constructive notice of bankruptcy for the purpose of the rules on set off.

4.181 The foregoing rules relate to set off between liquid debts. Under the doctrine known as "balancing of accounts in bankruptcy", the restriction noted above that an illiquid debt cannot be set off against a liquid debt is relaxed. The main policy reason is that it would be unjust to require a creditor of a bankrupt to pay a liquid debt in full while he received only a dividend for his illiquid (future, contingent or disputed) claim in the sequestration or trust deed.[3] So, subject to certain limitations,[4] the creditor in an illiquid claim against a bankrupt has a right to retain a liquid debt due by him to the bankrupt until his illiquid claim becomes a liquid debt, and then to set off the two debts.[5] One limitation is that the debt must have been acquired before notice of bankruptcy since, as in the case of compensation under the 1592 Act, there must be concourse of debit and credit before then.[6] We have proposed that in a debt arrangement scheme, the creditor in an illiquid (future, contingent or disputed) debt would be excluded from the scheme until the debt became liquid, and since the insolvent party is normally the debtor in the illiquid claim,[7] a question of balancing accounts in bankruptcy should in practice rarely arise in a scheme application. If the debtor were to raise an action for payment of a liquid debt against a party whose illiquid debt was excluded from a scheme, we think that the common law should determine whether a plea of retention with a view to eventual set off should be allowed, against the background of our recommendation that registration of a debt arrangement scheme would not imply constructive notice of insolvency.[8]

4.182 We **recommend:**

(1) No statutory rules are needed to regulate questions of compensation (set off) of liquid debts, or of retention of illiquid debts for the purpose

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[1]See *Encyclopaedia,* vol. 13, p. 13 (article by Gloag); Goudy, pp. 555–6; Erskine, *Institute,* III, 4, 18; Bell, *Commentaries, supra.*

[2]See Recommendation 4.38 (para. 4.267).

[3]Goudy, p. 550. A subsidiary reason is that retention by the bankrupt's creditor is inconsistent with the creditor's right to obtain a warrant for diligence in security of an illiquid claim due by the bankrupt.

[4]The plea of retention must not involve double ranking in the sequestration for the same debt, and the claim on which retention is pleaded must be acquired by the creditor in good faith and not involve a breach of a contract or fair understanding between the parties; *Encyclopaedia*, vol. 13, pp. 14 and 15.

[5]*Mill* v. *Paul* (1825) 4 S. 219; *Smith* v. *Lord Advocate* (*No. 2*) 1981 S.L.T. 19.

[6]*Mill* v. *Paul, supra*; *Taylor's Tr.* v. *Paul* (1888) 15 R. 313.

[7]Wilson, *Law of Scotland Relating to Debt* (1982) p. 191: cf. *Borthwick* v. *Scottish Widows Fund* (1864) 2 M. 595 where the insolvent party was creditor in an illiquid claim against an insurance company which had a liquid claim against him.

[8]See Recommendation 4.38 (para. 4.267).

of eventual compensation, in cases where one of the parties has applied for or obtained a debt arrangement scheme.

(2) In applying, however, the common law rule that compensation, or retention and compensation, of a debt due to an insolvent person against a debt due by him cannot be competently pleaded where there was no concourse of credit or debit before notice of bankruptcy, the registration of a debt arrangement scheme should not by itself be treated as giving such notice.
(Recommendation 4.26; clause 38(2).)

(e) *Debts secured by recourse against co-obligants*

4.183 The debtor may be liable along with a co-obligant, such as a co-debtor or cautioner (guarantor) in respect of the whole or part of a debt included in a debt arrangement scheme. Since many consumer as well as commercial debts are secured by guarantees granted by relatives, friends, workmates or business associates of the debtor, specific provision is necessary to deal with such problems as can be anticipated. A scheme may affect other kinds of co-obligants, moreover, such as wrongdoers jointly and severally liable in delict or persons jointly and severally liable as principals under contracts. In short, we are concerned here with any cautioner or other co-obligant who, on paying all or part of the debt, would acquire a right of relief against the debtor which he may wish to vindicate by claiming to be included in the debtor's scheme.

4.184 We think that a debt secured by a right of recourse against a co-obligant should be included in a debt arrangement scheme if and insofar as it was payable by the debtor but unpaid at the first notice date. It would be unfair to the co-obligant, and if the co-obligant were insolvent, possibly unfair to the creditor, to require the creditor to recover first from the co-obligant. Where the creditor had a "real security" granted by the debtor over his property as well as a "personal security" or right of recourse against a co-obligant, the debt should be excluded from the scheme unless and until the creditor discharged, realised or "foreclosed" the security as mentioned above.[1] This exclusion should not however apply where the real security had been granted over the co-obligant's property rather than the debtor's property.

4.185 On analogy with sequestration law, it should be provided by statute that any right of recourse by a creditor against the co-obligant should not be prejudiced by either (a) the inclusion of the creditor's debt in a scheme or the acceptance by the creditor of a disbursement under the scheme, or (b) the debtor's discharge from liability for the debt at the end of a scheme[2] (which would be of importance in a composition scheme).

4.186 If a co-obligant of a bankrupt pays the debt *in full*, he may require the creditor to grant an assignation of the debt to him and may then rank in the sequestration in subrogation for the creditor in respect of the right of relief to which he is entitled[3] and indeed may rank in the sequestration without

[1]Recommendation 4.23(2) (para. 4.174).

[2]Compare Bankruptcy (Scotland) Bill 1984, clause 57(1) replacing Bankruptcy (Scotland) Act 1913, s. 52.

[3]Goudy, pp. 562–3; Gloag and Irvine, p. 803 *et seq.*

obtaining a formal assignation.[1] On the other hand, if the creditor has ranked and drawn a dividend from the bankrupt's sequestration, a co-obligant who pays the *deficit* cannot rank in the sequestration, because to allow a second ranking of this type would give that particular debt a preference over other debts.[2] It appears to us that this common law rule against double ranking should apply *mutatis mutandis* in debt arrangement schemes. As we observed in our Report in Bankruptcy:[3]

> "From the point of view of other creditors, the bankrupt has incurred one debt and one debt only and the fact that the creditor has secured collateral obligations from another person should not entitle that debt to a double ranking."

We do not think that this matter can be left to the common law since the common law rule against double ranking only applies in those bankruptcy processes (such as sequestrations or trust deeds for creditors) where the debtor is divested of his estate, and not in processes (such as private composition contracts) where there is no divestiture.[4] We propose therefore that the implementing legislation should expressly provide that where after the first notice date a co-obligant pays the unpaid balance of the full amount of the debt (not the composition in a composition scheme) or if the co-obligant's liability is less than that of the scheme debtor, where he pays the unpaid balance of the full amount (not the composition) of the part of the debt for which he is liable, and thereby acquires a right of relief against the debtor, then the co-obligant may apply to the administrator to vary the scheme or draft scheme by subrogating him for the original creditor to the extent of his right of relief. In no other circumstances however should a co-obligant be entitled to have a claim of relief arising after the first notice date against the debtor included in a debt arrangement scheme. The foregoing rule should apply to schemes providing for payment of debts in full as well as composition schemes. The scheme may break down so that the debts may not in fact be paid in full, and to allow a co-obligant who had paid part of a debt to rank in a scheme in addition to, and not in place of, the original creditor would be to give that debt a preference in the disbursements under the scheme made before it broke down.

4.187 If the co-obligant paid part of the debt prior to the first notice date, the partial payment would be deducted from the amount of the debt for which the creditor ranked. The co-obligant's claim of relief against the debtor could then be included in the scheme since it would not infringe the rule against double ranking.[5]

4.188 The precise terms of a contract of caution may be held to exclude ranking on the principal debtor's estate by a cautioner e.g. where the cautioner has agreed not to prejudice the creditor in any competition or ranking process.[6] Moreover, where the cautioner's liability is less than that of the principal

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[1]Goudy, p. 562, footnote (d); Gloag and Irvine, *supra*.

[2]Goudy, pp. 561–2.

[3]Para. 16.27. A prohibition of double ranking in debt arrangement schemes was agreed on consultation: Consultative Memorandum No. 50, Proposition 23 (para. 2.68).

[4]Goudy, pp. 562–3; *Mackinnon* v. *Monkhouse* (1881) 9 R. 393.

[5]Compare *Thomson* v. *Latta* (1863) 1 M. 913, 920.

[6]*Harvie's Trs.* v. *Bank of Scotland* (1885) 12 R. 1141.

debtor, in construing the contract of caution a somewhat fine distinction is drawn between a cautioner's guarantee of the whole debt subject to limited liability on his part (which is construed as precluding ranking by the cautioner on the principal debtor's estate to enforce his right of relief)[1] and a guarantee of part only of the debt (which is not so construed).[2] Accordingly the legislation allowing subrogation in a scheme by a co-obligant to vindicate a right of relief should not override any agreement expressly or impliedly prohibiting the co-obligant from claiming subrogation.

4.189 Where the co-obligant had paid the unpaid balance of the whole debt, he would rank in place of the creditor on the whole future disbursements under the scheme which would otherwise have been paid to the creditor. Where the co-obligant's liability was less than that of the scheme debtor and he paid the whole amount of the part of the debt for which he was liable, we propose that he and the original creditor would rank on the original creditor's share of future disbursements in such proportions as would secure, so far as practicable, that the amounts to which they were entitled under the scheme were satisfied at the same time. The following example may illustrate the principle involved.

EXAMPLE

Scheme provides for composition of 50%

Debt due by scheme debtor to original creditor	£1,000
∴ sum due to original creditor under scheme	£ 500
less amount already disbursed by administrator	£ 100
leaves amount due to the original creditor under the scheme	£ 400
Total liability of co-obligant to original creditor duly paid	£ 600
∴ sum due to co-obligant under scheme (50%)	£ 300
∴ sum due to original creditor under scheme (£400–£300)	£ 100

∴ creditor and co-obligant rank on future disbursements of the original creditor's share in the scheme in the proportions of 25% to the original creditor and 75% to the co-obligant.

The foregoing example also illustrates the principle that the creditor receives the full benefit of his right of recourse against the co-obligant (£600) plus a composition of the balance of the £1,000 debt from the scheme, (50% of £400=£200) while the co-obligant receives a composition of his right of relief (50% of £600=£300). In cases where the original creditor's debt had been included "late", the sums due in terms of the scheme would be satisfied partly by disbursements by the administrator under the scheme and partly by payments under a decree such as we recommend above.[3] However, the disbursements made by the administrator would be apportioned in the proportions just mentioned since the implementing legislation would require such apportionment to be made "so far as practicable".

4.190 It would be both unnecessary and undesirable to attempt to make

[1] *Idem.*
[2] *Veitch* v. *National Bank of Scotland* 1907 S.C. 554.
[3] Recommendation 4.17(3) (para. 4.143).

comprehensive statutory provision regulating the very complex rights and liabilities of a creditor, scheme debtor and co-obligants in cases where one or more of the co-obligants is or are also insolvent. Apart from the prohibition of double ranking, the leading common law principle is that the creditor may rank on all the bankrupt estates simultaneously provided that he does not draw more than 100p in the pound in all.[1] We think that the courts would apply this principle where one or more of the insolvent co-obligants obtained a debt arrangement scheme and that legislation is unnecessary.

4.191 The "late" inclusion in confirmed schemes of debts owed to contingent and other creditors would, under our proposals, normally be a matter to be decided by the sheriff in his discretion. We think, however, that where inclusion was merely a matter of a co-obligant replacing wholly or partially a creditor already included in a confirmed scheme, then the administrator should be entitled to effect the subrogation on a simple application by the co-obligant.[2] We have already proposed that a contingent creditor should have an option to stay out of a scheme and enforce his debt in full on the termination of the scheme or to apply for late inclusion and these options would be available to a co-obligant having a right of relief. A co-obligant, however, should be put to his choice between those options within a short period after making the payment entitling him to subrogation. The reason for this is that the creditor, on receiving payment of the full amount of his debt from the co-obligant, or the administrator and co-obligant, would be required (as recommended above[3]) to intimate that fact to the administrator who would then be obliged to cease disbursements to that creditor and to apply to the sheriff to vary the scheme by excluding the debt. But the exclusion of the debt would not be appropriate if a co-obligant elected to be included in a scheme and became entitled to rank on future disbursements in subrogation for the original creditor. We think therefore that a co-obligant should be entitled to be subrogated for the creditor to the extent of the amount due to him under his right of relief only if he applied to the administrator for subrogation within a short period, say 14 days, after making the payment, or last payment, by virtue of which he became entitled to rank in the scheme.

4.192 On the model of the procedure proposed for excluding debts from draft schemes before confirmation,[4] there should be a simple administrative procedure for the adjustment by the administrator of a draft scheme where subrogation was applied for before confirmation.

4.193 We **recommend:**

(1) A creditor's right of recourse against a scheme debtor's co-obligant should not be affected by the inclusion of the debt in a scheme, or by the creditor's acceptance of a disbursement under the scheme, or by the discharge of the debtor's liability to the creditor at the end of a scheme.

(2) Where after the first notice date:

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[1]Goudy, pp. 563–4.

[2]This would be modelled on the procedure proposed at paras. 4.277 and 4.288 below for subrogating the assignee of a debt in place of the original creditor.

[3]Recommendation 4.19 (para. 4.153).

[4]See Recommendation 4.19(5) (para. 4.153).

(*a*) a co-obligant pays the unpaid balance of the full amount of the debt (not the composition in a composition scheme); or

(*b*) if the co-obligant's liability is less than that of the scheme debtor, where the co-obligant pays the unpaid balance of the full amount (not the composition) of the part of the debt for which he is liable,

and thereby acquires a right of relief against the scheme debtor, then the co-obligant may apply to the administrator to vary the scheme or draft scheme by subrogating him for the original creditor to the extent of his right of relief. In no other circumstances should a co-obligant be entitled to have a claim of relief, acquired after the first notice date against the debtor, included in a debt arrangement scheme.

(3) Where the co-obligant's claim of relief arises by virtue of his payment of part of the debt, he should rank along with the original creditor on the original creditor's share of future disbursements under the scheme in such proportions as will secure, so far as practicable, that the sums due to the original creditor and the co-obligant under the scheme are satisfied at the same time.

(4) The common law should regulate questions of ranking where one or more of the co-obligants is or are insolvent.

(5) There should be a simple procedure whereby the administrator could effect the subrogation of a co-obligant in the creditor's place in a draft scheme or confirmed scheme.

(6) A co-obligant should be required to make his election between subrogation in a confirmed scheme and remaining outside the scheme, within a short period (say 14 days) after the payment was made by virtue of which he became entitled to subrogation.

(Recommendation 4.27; clauses 27(6), 28(4)(*b*) and 34.)

(8) Debts due under regulated agreements and related securities under Consumer Credit Act 1974, and unregulated hire purchase and conditional sale agreements

4.194 *Existing law*. Though the effect of sequestration on regulated agreements and securities under the Consumer Credit Act 1974, and on judicial orders under Part IX of that Act controlling the enforcement of such agreements, is not specifically regulated by statute, some provision seems necessary in the context of debt arrangement schemes. Hire purchase and hire contracts and other credit transactions involving reservation of title or the grant of a security normally provide that the creditor or owner may terminate the agreement and exercise other contractual remedies (such as acceleration of payments and repossession of goods) in the event of the debtor or hirer becoming notour bankrupt (in future, "apparently insolvent") or being sequestrated or granting a trust deed for creditors or entering into a composition contract,[1] and such a provision would normally in future include an application for a debt arrangement scheme.[2] (The agreement may alternatively provide that such states of bankruptcy terminate the agreement *ipso facto*.) Other credit agreements (e.g. loan agreements) not involving reservation of title or a security may provide for such contractual remedies as

[1]E.g. Gow, *The Law of Hire Purchase in Scotland* (2nd edn.), p. 196.

[2]See Recommendation 4.46(1) (para. 4.311).

acceleration of payments in the event of insolvency. Under the 1974 Act the creditor must give written notice of seven days before exercising his remedies.[1] Since insolvency is not a remediable breach of contract, an insolvent debtor cannot prevent the running of the period of notice, but he may apply to the court for judicial control of enforcement under Part IX of the 1974 Act.

4.195 Judicial control of regulated agreements under Part IX is exercised mainly through the following orders:

(1) A *time order under section 129(2)(a)* for payment by instalments by the debtor or hirer or a surety (guarantor) of sums owed under *any regulated agreement or a security* (e.g. a guarantee) (i.e. arrears owed at the time when the order is made);

(2) A *time order under section 129(2)(a) and 130(2)* for payment by instalments by such a person of future sums due under a *regulated hire purchase or conditional sale agreement* which, though not payable by the debtor at the time when the order is made, would if the agreement continued in force, become payable under it subsequently;

(3) A *time order under section 129(2)(b)* for the remedying by the debtor or hirer within a specified period of any *non-monetary breach* of a regulated agreement;

(4) An *order under section 130(6)* varying or revoking a time order;

(5) An *order under section 131 protecting property* of the creditor or owner under a regulated agreement *pending proceedings* under the 1974 Act;

(6) An *order for financial relief of a hirer under section 132* (for repayment of sums paid by the hirer, or reducing or extinguishing sums owed by the hirer) available when the owner has recovered possession of the goods without an action or obtains a delivery order in an action;

(7) A *"return order" under section 133* for the return of any goods comprised in a *regulated hire purchase or conditional sale agreement* (not merely "protected goods") or a *"transfer order" under section 133* (a "split order") for the transfer of title to the debtor of some goods and the return of the remainder to the creditor;

(8) An *ancillary order under section 135(1)* attaching conditions to, or suspending the operation of, any term of a (statutory or common law) order made in relation to a regulated agreement;

(9) An *ancillary order, for variation of an agreement, under section 136* which provides that the court may "make such provision as it considers just for amending any agreement or security in consequence of a term of the order";

(10) A *combination of some of the above orders*, e.g. the equivalent of a postponed order for specific delivery under the Hire Purchase (Scotland) Act 1965 would be a return order under section 133 suspended under section 135 pending compliance with a time order under section 129(2)(*a*).

4.196 A time order under section 129(2)(*a*) would not, by itself, prevent the owner or creditor from exercising his contractual remedies of termination or

[1]1974 Act, ss. 76 and 98.

repossession of "unprotected goods" on the debtor's insolvency but an ancillary order under section 136 varying the agreement or a return order under section 133 (relating to goods held under a regulated hire purchase or conditional sale agreement) suspended under section 135 pending compliance with a time order, or a common law decree for delivery (e.g. relating to goods held under a regulated consumer hire agreement) suspended by an order under section 135 pending such compliance, might do so.[1] In the case of a time order relating to a regulated hire, hire purchase or conditional sale agreement, where the debtor or hirer is in possession of the goods, he is treated as "a custodier of the goods under the terms of the agreement" (if title has not passed to him) even though the agreement has been terminated.[2] In such a case, the effect of the time order is not to revive the terminated agreement but rather to create a new statutory agreement which has the same terms as the original agreement, except as regards payment obligations regulated by the time order and except as varied by the court under section 136, and which has effect for so long as the debtor retains possession, apparently even if the time order is later revoked.[3] It will be seen that time orders under section 129(2)(*a*) for payment by instalments which could be superseded by a scheme may be associated with orders (relating for example, to the possession, ownership or delivery of goods comprised in a regulated agreement) which cannot be readily superseded by a scheme. Further, the practical effect of certain orders under Part IX of the 1974 Act may be to prevent the inclusion of debts in a scheme where under our proposals it is a condition precedent of inclusion that the creditor should first exercise or waive his contractual remedies (e.g. security rights[4]).

4.197 *Secured debts due under regulated agreements.* We have recommended[5] that a debt secured by a contractual security over property of the debtor (such as a heritable security or pledge) should be excluded from a scheme unless and until the security was discharged, or the secured property realised or acquired in default of sale in partial satisfaction of the debt. In principle we think that this rule should apply to debts due under regulated agreements secured by a contractual security over the debtor's property. The enforcement of the security would continue to be subject to the provisions of the 1974 Act, including those on judicial control in Part IX of the Act. For so long as the secured debt was not included in a scheme, existing orders under the 1974 Act would continue in operation after confirmation of the scheme. If an order under Part IX was applied for after confirmation of the scheme, the sheriff's decision whether or not to make the order would be reached in the light of the existence of the scheme.

4.198 *Unsecured debts due under regulated agreements.* In the case of unsecured debts due under regulated agreements, we think that since a debt arrangement scheme would apply in principle to all such debts once they became payable and undisputed, the debtor's obligations of payment should so far as practicable be regulated by the debt arrangement scheme rather than

[1]Goode, "The Consumer Credit Act 1974", [1975] C.L.J. 79, 117–8.
[2]1974 Act, s. 130(4).
[3]Goode, *The Consumer Credit Act* (1979) p. 326.
[4]See Recommendation 4.23(2) (para. 4.174).
[5]*Idem.*

by a monetary time order under section 129(2)(*a*) of the 1974 Act. The debtor's admitted insolvency would create a new situation. It would be anomalous if an unsecured debt subject to a time order was always excluded from a scheme with the result that the unsecured creditor was not bound by the general composition of debts under the scheme.

4.199 *Debts under hire purchase and conditional sale agreements*. Since most hire purchase and conditional sale agreements entered into by a debtor subject to a debt arrangement scheme will be regulated under the 1974 Act, we have found it convenient to deal with such agreements here, though our proposals relate to unregulated agreements as well as regulated agreements. We have considered three options on debts due under hire purchase and conditional sale agreements. First, to focus discussion on a solution adopted or proposed in other countries,[1] we sought views in our Consultative Memorandum No. 50[2] on whether the creditor should be compelled to elect between his remedy of repossession and his remedy of claiming sums due under the contract by ranking in the scheme, but having used one remedy, he would be barred from using the other. The argument for this approach is that repossession, while causing hardship to the debtor, is often of little value to the hire purchase creditor.[3] On consultation, the few who commented rejected this solution. The Scottish Association of Citizens Advice Bureaux thought that it would be unfair to the creditor, unduly reducing his property rights. The Law Society of Scotland thought that if the debt arrangement scheme provided for payment in full, the hire purchase creditor should be required to rank in the scheme, but that if it provided only for a composition, the creditor should be entitled to rank in the scheme in respect of any deficit arising after re-sale of the repossessed goods: in no circumstances, they said, should the creditor be obliged to elect between the two remedies. In our view, the safeguards in the 1974 Act must be taken as adequately protecting hire purchase debtors and there seems no reason why hire purchase debtors fortunate enough to obtain a scheme should be in a better position than other hire purchase debtors.

4.200 Second, we considered whether a hire purchase creditor[4] should be obliged to rank for arrears accrued to the first notice date, since a hire purchase agreement is not a form of security in strict law. Under this option, if payments outside the scheme were kept up but further default then occurred, the hire purchase creditor could exercise his contractual remedies including repossession and realisation[5] and opt either to rank in the scheme for the deficit on realisation or stay out of the scheme and enforce the deficit in full after termination of the scheme. We reject such a solution as unduly complex requiring complicated provisions on, for example, whether or how the net proceeds of sale of the repossessed goods should be ascribed to the arrears originally included in the scheme or to the sums for which the creditor had not yet ranked in the scheme. Furthermore, a time order and other orders

[1]E.g. U.S. Bankruptcy Report, pp. 165–6; Tassé Report in Canada, pp. 93–4; A.L.R.C. Report No. 6, pp. 28–30; Draft E.E.C. Directive No. C80/7 of 27.3.1979, article 9.

[2]Paras. 2.56 to 2.63, Proposition 19.

[3]Crowther Report, para. 6.6.45. Most goods taken on hire purchase are motor vehicles or household goods and the repossession value is generally low: *ibid*, para. 6.6.46.

[4]The same considerations apply to creditors in conditional sale agreements.

[5]Subject in the case of a regulated hire purchase agreement to judicial control under the 1974 Act.

under the 1974 Act would be applicable only to the sums for which the creditor had not yet ranked in the scheme and it is not easy to see how this would work in practice.

4.201 We propose therefore the adoption of a third solution, namely that sums due under a hire purchase (or conditional sale) agreement should not be included in a scheme unless and until (*a*) the agreement had been terminated, and (*b*) if by virtue of section 130(4) of the 1974 Act the debtor were treated as a "custodier of the goods under the terms of the agreement",[1] until he ceased to be so treated. The effect would be that a hire purchase creditor would not rank in a scheme for arrears of hire purchase instalments until the hire purchase agreement was terminated. On termination we would expect that the hire purchase creditor would exercise the normal contractual remedies of acceleration of payments and repossession and realisation of goods comprised in the agreement, and rank for any deficit on realisation. If, however, the debtor in the hire purchase (or conditional sale) agreement fell to be treated as a "statutory custodier of the goods under the terms of the agreement" by virtue of section 130(4) of the 1974 Act for so long as he retained possession of the goods without becoming owner of them, there would in effect be a new statutory agreement corresponding to the original agreement (except as regards payment obligations regulated by a time order under section 129(2)(*a*) and except as varied under section 136) but not terminable by the creditor so that the creditor could not exercise his contractual remedies of repossession or realisation of the goods. In such a case, we envisage that the creditor would apply for a return order or a transfer order under section 133(1) or a common law order for delivery of goods to the creditor having the effect of terminating the new statutory agreement.[2]

4.202 *Effect of scheme on orders under 1974 Act, Part IX* .Where a debt subject to a time order for payment by instalments under section 129(2)(*a*) of the 1974 Act was included in a scheme, either on confirmation of the scheme or on variation of the scheme in a creditor's application to include the debt, the confirmation order or variation order as the case may be should have the effect of revoking the time order. An application for revocation of the time order should be unnecessary. To avoid inconsistent dual regulation of instalment payments by a scheme and a time order, it should be incompetent for the court to make a time order relating to an included debt while the scheme was in force and it should be provided by act of sederunt that any application by the debtor for a time order should state that the debt concerned was not included in a scheme.

4.203 The foregoing rules of inclusion and automatic revocation would apply to cases where only a time order for payment by instalments under section 129(2)(*a*) (or that section as read with section 130(2)) of the 1974 Act was involved. In more complicated cases involving, in addition to a time order under section 129(2)(*a*), other types of order, (such as a time order under section 129(2)(*b*) for remedying a non-monetary breach, or a return order, or a transfer order, or an order suspending the exercise of contractual

[1]See para. 4.196 above for an explanation of this expression.

[2]In some cases, the creditor may also have to apply for the revocation of a time order as proposed in para. 4.203 before the debt could be included.

remedies, or imposing conditions, or varying a regulated agreement, or one or more orders of those types combined with an instalment time order[1]), it would not be right to lay down any rule revoking the order on inclusion of the debt since such orders apply or may apply to matters other than the payment of debts. In such cases, we think that to avoid inconsistent dual regulation of payment by a monetary time order and a scheme, the debt should not be included in the scheme unless the creditor obtains from the court an order under section 130(6) revoking the monetary time order. Moreover, consequential provision would be needed under which, where a scheme application was pending or a scheme had been confirmed and the creditor applied for revocation of a monetary time order, the court would have an express power, on revoking the time order, to vary or revoke any other order made in relation to the debt, or to the agreement under which the debt was owed, under sections 129(2)(*b*), 131, 133, 135 or 136 of the 1974 Act. Thus for example, if a return order or common law delivery order had been suspended under section 135 pending compliance with a time order under section 129(2)(*a*), the court on revoking the time order could revoke the suspension order under section 135 so as to make the return order or delivery order have immediate effect.

4.204 *Orders for financial relief of hirer.* Under the 1974 Act, section 132, where the owner under a regulated consumer hire agreement recovers possession of the goods without an action or the sheriff orders delivery of the goods to the owner, the sheriff may *inter alia* make an order that the obligation to pay the whole or any part of a sum owed by the hirer to the owner in respect of the goods should cease. We propose that where at the first notice date an application under the 1974 Act, section 132 or an action for delivery of goods under a regulated consumer hire agreement was pending, the debt should be excluded from the scheme until the application or action was disposed of and it was known what the amount of the debt will be.[2] If a debt subject to a regulated consumer hire agreement had already been included in a draft scheme or a confirmed scheme, and the sheriff subsequently ordered under section 132 that the obligation to pay the debt should cease, we envisage that the rules relating to the payment of debts outside a scheme described above[3] should apply.

4.205 We **recommend:**

(1) Where a debt secured by a contractual security over the property of the debtor was payable by the debtor under a regulated agreement under the Consumer Credit Act 1974, or under a related "security" (e.g. a guarantee), it should be excluded from a scheme in accordance with the general rule on secured debts recommended above.[4] Time orders and other orders under the 1974 Act relating to the debt should

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[1]See para. 4.195 above.

[2]This is the same as the solution for orders re-opening extortionate credit agreements proposed at paras. 4.132 to 4.133 above, except that in the case of a regulated consumer hire agreement, the hirer must be allowed to apply for relief after the first notice date in his scheme application since his right to apply for relief may not arise till after that date when the creditor delays recovery of possession or a possessory action.

[3]See paras. 4.149 *et seq.*

[4]Recommendation 4.23(2) (para. 4.174).

not be affected by the scheme unless and until the debt was included in the scheme. The same rules should apply to debts under regulated agreements being enforced by adjudications or enforceable by poinding of the ground.[1]

(2) A debt due by the debtor under a hire purchase or conditional sale agreement, whether regulated under the 1974 Act or not, should be excluded from a scheme unless and until (*a*) the agreement had been terminated and (*b*) if by virtue of section 130(4) of the 1974 Act the debtor were treated as custodier of the goods in terms of the agreement, until he ceased to be so treated.

(3) Where a debt was subject to a time order for payment by instalments under section 129(2)(*a*), or that section as read with section 132, of the 1974 Act, then:

(*a*) if another order relating to the debt, or to the agreement under which the debt is owed, was in force, being an order made under:

section 129(2)(*b*) (remedying by debtor or hirer of a non-monetary breach of agreement);

section 131 (protection order);

section 133 (return order or transfer order relating to goods comprised in a regulated hire purchase or conditional sale agreement);

section 135(1) (order attaching conditions to, or suspending the operation of, any order made in relation to a regulated agreement); or

section 136 (variation of agreements or securities),

the debt should be excluded from the scheme until the order under section 129(2)(*a*) had been revoked under section 130(6) or had otherwise ceased to have effect;

(*b*) if another order mentioned in the foregoing list relating to the debt or agreement is not in force, the debt may be included in the scheme on its confirmation or by variation, and the order confirming or so varying the scheme should have the effect of revoking the order under section 129(2)(*a*).

(4) Where a scheme application was pending or a scheme had been confirmed and the court revoked a time order under section 129(2)(*a*), the court should have power to vary or revoke any other order mentioned in paragraph 3(*a*) above made in relation to the debt, or the agreement under which the debt was due.

(5) In the case of a debt due by the debtor as hirer under a regulated consumer hire agreement, where at the first notice date an application under the 1974 Act, section 132(1) (financial relief of hirer), or proceedings in which the court may make an order under section 132(2), were pending, the debt should be excluded from the scheme until the application or proceedings were disposed of.

(Recommendation 4.28; clauses 15(5)(*a*) and (*b*), 15(6), 18(5)(*c*), 23(1)(*f*) and (*g*), 28(1)(*f*) and (*g*), 28(5), Schedule 7, paragraph 21.)

[1]Recommendations 4.14(3) (para. 4.118) and 4.24(2) (para. 4.176).

(9) Preservation of creditors' other rights and remedies

4.206 In general, we consider that an interim order sisting diligence and a debt arrangement scheme should not affect the rights and remedies for enforcing payment of debts other than the ordinary modes of diligence applicable to unsecured debts. Accordingly, we propose that any legislation following on this report should expressly "save" such rights or remedies. This would preserve not only the security and other rights discussed above but also remedies which, though not given by law expressly for the purpose of enforcing debts, are in fact used for that purpose. Such remedies include the threat of disconnection of supply of gas and electricity for non-payment of charges, and ejection and removing for non-payment of rent.[1]

4.207 *Gas and electricity charges.* The British Gas Corporation and the electricity boards should be required to rank in the debt arrangement scheme for arrears of gas and electricity charges accrued to the first notice date. In the case of the supply of gas or electricity to the debtor's residence, we would expect that the administrator in preparing the scheme would make allowance to the debtor of sufficient income to keep up payments of gas and electricity for his residence as these would be part of normal "necessaries".

4.208 There should not however be any restraint on the fuel boards' powers of disconnection.[2] Under their Code of Practice, the fuel boards will not disconnect supply if the defaulting customer agrees to make regular payments for future supply and to pay off arrears in reasonable instalments. These arrangements are not unlike those under a debt arrangement scheme with the difference that in a composition scheme, the arrears would not be payable in full. It should be for the fuel boards to determine in a particular case whether there was a sufficient ground for discontinuance of future supply.

4.209 In relation to subsequent default, the fuel boards would have the same rights as a "subsequent creditor" or contingent creditor to apply for late inclusion, or revocation, or to wait till after the termination of the scheme and to enforce their subsequent debts in full.

4.210 *Rent.* In general, the same solution should apply to rent arrears as to fuel debts. A landlord should rank in a debt arrangement scheme for rent arrears accrued before the first notice date and should be entitled to apply to have arrears arising after that date included in a scheme. Where the rent related to the debtor's residence, and no court proceedings for recovery of possession had been initiated, it would be assumed in preparing the scheme that the debtor would keep up payments outside the scheme; and, where the rent related to property other than the debtor's residence, the fact that the landlord might terminate the lease might be relevant in determining whether a debt arrangement scheme should be confirmed.

4.211 In some cases, an action by the landlord for recovery of possession of the debtor's residence for non-payment of rent might already have been commenced, and this may have been adjourned under the Tenants' Rights Etc. (Scotland) Act 1980 or the Rent (Scotland) Act 1984 to allow an

[1]The background law on these topics is described at paras. 3.103 *et seq.* in the context of time to pay decrees and orders.

[2]As to these powers, see para. 3.115 above.

arrangement for payments of arrears to have effect. In some of these cases the arrangement may have been imposed by the court as a condition of the adjournment.[1] As mentioned in Chapter 3,[2] however, in some courts it is common practice, at least in cases under the 1980 Act, to use such an adjournment merely as a trial period to determine whether or not the debtor is able and willing to make regular payments towards his arrears: if the trial is successful, the action is then sisted on the basis of an informal arrangement between the debtor and his landlord.

4.212 The existence of any of these arrangements would have to be taken into account in deciding whether to make a debt arrangement scheme; but, if a scheme were made, there would then be a question as to what effect that scheme should have on any arrangement in the possessory action. In our view, the inclusion of rent arrears in the debt arrangement scheme should not prejudice any right which the landlord might have to seek a possessory decree in a court action, and it would then be for the court entertaining that action to determine in the circumstances of the case whether the action should be adjourned or sisted to allow payment of arrears through the debt arrangement scheme to be made or whether a possessory decree should be granted.

4.213 We **recommend:**

(1) Any legislation introducing debt arrangement schemes should make it clear that an interim order sisting diligence and a scheme would not affect creditors' remedies other than the diligences enforcing unsecured debts.

(2) In particular, such an order or scheme should not affect the rights of the electricity and gas boards to discontinue supply to a defaulting customer nor the right of a landlord to recover possession for non-payment of rent.
(Recommendation 4.29; clause 41.)

(10) Effect of scheme on negative prescription of debtor's obligation to pay

4.214 Under the law on negative prescription,[3] an obligation to pay a debt is extinguished if a "relevant claim" (such as the raising of a court action or the execution of diligence[4]) is not made by the creditor, or the debtor does not "relevantly acknowledge" the subsistence of the obligation, for a continuous period of five or 20 years (according to the kind of debt). If the prescriptive period is "interrupted" by such a claim or acknowledgement, the part of the prescriptive period which had already elapsed is cancelled and a new prescriptive period commences from the date of interruption. Under bankruptcy legislation, a creditor's petition, or the submission of a claim by a creditor, in a sequestration interrupts prescription on the creditor's debt,[5] and we considered whether the procedures for inclusion of a debt in a debt arrangement scheme should also have the effect of interrupting prescription.

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[1]See 1980 Act, s. 15(1).

[2]See para. 3.107.

[3]Prescription and Limitation (Scotland) Act 1973, ss. 6 and 7.

[4]*Ibid.*, s. 9(1).

[5]*Ibid.*, s. 9(1)(*b*) as originally enacted; and as amended by the Bankruptcy (Scotland) Bill 1984, Sched. 7, para. 3.

It would however be difficult and complex to list all the acts which should be treated as interrupting prescription: for example, should the list include objections by an excluded creditor to a scheme application or applications for revocation of a scheme? Moreover, such a list would not cover all the cases of creditors who would require protection from the running of prescription. For example a creditor holding a warrant for diligence omitted from a scheme for whatever reason should, we have proposed, have the option (which is not available in sequestrations) of staying out of the scheme and enforcing his debt in full after termination of the scheme or of applying for late inclusion. In the meantime he could not interrupt prescription by diligence. A debt arrangement scheme may subsist for three years and in some cases five years, with minor further extensions and, especially in the case of debts subject to the short negative prescription of five years, the dangers are obvious. It would be wrong to encourage a creditor to take steps, such as objecting to a scheme or applying for revocation of a scheme, simply to interrupt prescription.

4.215 In these circumstances we propose the adoption of a different approach. Section 6(4)(*b*) of the Prescription and Limitation (Scotland) Act 1973 provides that in computing the short negative prescriptive period, any period during which the creditor is under legal disability (by reason of nonage or unsoundness of mind[1]) shall not be reckoned as, or as part of, the prescriptive period. The disability does not "interrupt" the prescriptive period (in the technical sense of cancelling the old period and starting a new period[2]) but lengthens the prescriptive period by the period of legal disability. We consider that a similar principle should apply to debt arrangement scheme proceedings with the effect of lengthening the period of both the short and the long negative prescriptions.

4.216 We **recommend:**

In computing the short negative prescriptive period of five years under section 6 of the Prescription and Limitation (Scotland) Act 1973, and the long negative prescriptive period of 20 years under section 7 of that Act, none of the following periods, namely:

(*a*) the period after the first notice date while a scheme application was pending;

(*b*) the period when the sheriff's order disposing of a scheme application was appealable or subject to appeal;

(*c*) the period while a scheme was in force,

should be reckoned as, or as part of, the prescriptive period. (Recommendation 4.30; Bill, Schedule 7, paragraph 18.)

Section E. Functions, recruitment etc. of administrators of debt arrangement schemes

4.217 Because of the central position of the administrator in preparing and obtaining confirmation of a draft scheme and thereafter in promoting the smooth operation of the scheme and keeping it under review, it would be essential to ensure that suitable persons are appointed to act as administrators.

[1]1973 Act, s. 15(1).
[2]1973 Act, s. 6(5).

4.218 In allocating functions as between the sheriff and the administrator, regard must be had to the fact that there are no "judicial officers" within the Scottish Court Service equivalent to the English High Court masters or county court registrars. Accordingly, we propose that the main decisions and orders on the confirmation, variation, and termination of a scheme, and the discharge of the debtor, should be made by the sheriff.

4.219 The main functions of the administrator would thus be executive or procedural rather than "adjudicatory" in character. In summary, these functions would include those in the following list (which is not exhaustive):

(i) to intimate to creditors copies of the interim order sisting diligence;

(ii) to interview the debtor and explain the nature of the procedure and the debtor's rights and duties in connection with it;

(iii) to check the statement of affairs lodged with the debtor's application and to interview the debtor to ascertain his financial position; if necessary to prepare a new statement of affairs;

(iv) to check that the application is within the statutory limits of competence and may be entertained by the sheriff;

(v) in appropriate cases to obtain the sheriff's authority for an advertisement for creditors' claims or for valuation of items of the debtor's property and, if necessary, to obtain an undertaking from the debtor not to remove or dispose of items of property;

(vi) to assess whether a scheme was feasible, i.e. that the debtor would be likely to comply with a scheme;

(vii) after such informal contacts, if any, with creditors as he thought fit, to serve on creditors a formal notice inviting them to verify their debts or to claim interest;

(viii) to explain to the debtor the various types of scheme (extension of time, composition, or combined extension and composition) and, in consultation with the debtor, to prepare a draft scheme containing the debtor's proposals for payment, and to serve it with relative documents on creditors and co-obligants;

(ix) where appropriate, to adjust the draft scheme by including omitted debts, or excluding newly satisfied debts or subrogating co-obligants or creditors' assignees and if necessary to re-serve the adjusted scheme;

(x) on receipt of any objections to the scheme, to ascertain whether agreement can be obtained as between the parties and, if not, to arrange a hearing before the sheriff;

(xi) to attend a hearing on objections or any other hearing before the sheriff and to intimate the sheriff's decisions and orders;

(xii) to receive payments from the debtor under a scheme and to disburse them in dividends to the creditors periodically;

(xiii) to keep the operation of the scheme under review;

(xiv) to make reports, on request, to the creditors included in the scheme on the manner in which the debtor was performing his obligations under the scheme;

(xv) to supervise, and to report to the sheriff on, the debtor's compliance with a provision of the scheme requiring disposal of items of property;

(xvi) to deal with the subrogation in the scheme of assignees of creditors and co-obligants of the debtor, and to perform any necessary functions in connection with applications for variation or revocation of a scheme;

(xvii) to contact the debtor if he defaults, ascertain the reason for default, and if necessary apply to the sheriff for variation or revocation of the scheme;

(xviii) to apply to the sheriff for the debtor's discharge on the termination of a successful scheme; and

(xix) to comply with any regulations on obtaining his own discharge from the office of administrator.

4.220 In our Consultative Memorandum No. 50, we invited views on the type of person who should be eligible for appointment as administrator, and in particular whether they should be sheriff clerks or full-time officials of the sheriff clerks' departments or unpaid, part-time volunteers appointed from a list of persons recruited from the community.[1] On consultation, reactions were divided. The Scottish Association of Citizens Advice Bureaux said that the administrator should not be a Citizens Advice Bureau volunteer because "the post needs a full-time commitment. Secondly, the job capability includes executive functions which are totally alien to advice givers. Lastly, the job if filled by CAB volunteers would prejudice the impartiality and approachability of the CAB service". In their view, an administrator would have to be a court official on a similar grade to a sheriff clerk.

4.221 The Society of Messengers-at-Arms and Sheriff Officers pointed out that some officers of court already operate informal debt arrangement schemes, or debt pooling arrangements, for both consumer and commercial debtors; that they had deep knowledge and experience of debtors and debt problems; and that they were well placed to keep schemes under review because they already make visits periodically to debtors in their area.

4.222 The Law Society of Scotland thought that, while it might be possible to secure a debt counselling service by way of volunteers, a debt arrangement scheme system requiring a service of volunteer administrators would not be practicable. The Law Society did not think that the sheriff court staff, as presently organised, could accept the additional burden of operating the schemes. Apart from certain specialists in bankruptcy and liquidation, they would require extensive training on such matters as assessing whether a scheme should be made (having in mind the specialities of bankruptcy preferences, which the Society argued should apply in debt arrangement schemes, and of gratuitous alienations and fraudulent preferences) and adjudicating on claims. They suggested therefore that the administrator should be a chartered accountant specialising in bankruptcy work, possibly supplemented in the remote areas by solicitors. The costs of administration would be a charge on the debtor's payments, or in cases where the scheme was not confirmed, or broke down, or yielded insufficient income, by the Exchequer.

[1]Proposition 34 (para. 2.134).

4.223 The Scottish Law Agents Society was sceptical of the need for debt arrangement schemes, and pointed to the increase in the pressure on the time of the sheriff and court staff, which was already severe in many areas. They thought it necessary to ensure that a large additional bureaucracy should not emerge and tentatively suggested that administrators should be recruited from local authority social work departments.

4.224 We note that the Hughes Report on *Legal Services in Scotland* recommended that high priority should be given to developing a money management counselling service in Scotland, in consultation with Citizens Advice Bureaux and social workers.[1] Such a service might provide ultimately a source for the recruitment of persons qualified to act as administrators, but since it is not known whether or when the proposal will be implemented, other provision would require to be made at least in the meantime.

4.225 While we appreciate the difficulties involved in securing sufficient training for sheriff clerks, and while we acknowledge that the resources of the sheriff court are under pressure, we are firmly of the view that the function of administrator should, at least in the normal case, be performed by the sheriff clerk, or a member of his department. The sheriff clerk has easy and regular access to the sheriff; he has an existing staff, office facilities, record system, and an accounting system subject to government audit; he already collects instalments under criminal fines orders and compensation orders and in the latter case makes disbursements to members of the public.[2] It is envisaged that in cases where the debtor's affairs were complicated by gratuitous alienations, or unfair preferences, or by other factors, the sheriff could refuse the application.

4.226 There was no dissent on consultation from the suggestion that administrative duties of this kind would not be the best way of employing the skills of social workers, especially as they are already over-extended by their present duties. They might be regarded by creditors as over-sympathetic to debtors and conversely their relationship with their client—the debtor—might be prejudiced. Provision of administrators should not be a local authority function since the local authority will often be an important creditor. The appointment of a sheriff officer would be regarded by some as inconsistent with his duty of executing diligence, which he may require to do if a scheme is revoked. We doubt whether funds would be available to pay professional fees to chartered accountants and solicitors, and without adequate remuneration, they would have little incentive to act.

4.227 While we think that sheriff clerks or their subordinates would normally require to act as administrator, we think that it should be possible for the Secretary of State for Scotland, perhaps after experience of the working of the legislation has been obtained, to make one or more statutory instruments enabling other manpower resources to be tapped, whether throughout

[1](1980; Cmnd. 7846) para. 12.10: the Report recommends that the function of developing the service is to be entrusted to a newly constituted Legal Services Commission. The C.R.U. Debt Counselling Survey (1980) contains a wealth of valuable information on the existing "generalist" and specialist debt counselling agencies in Scotland.

[2]If our recommendations on conjoined arrestment orders in Chapter 6 were implemented, he would perform similar duties under such orders.

Scotland, or in particular sheriffdoms or sheriff court districts. Following the making of the statutory instrument relating to a court district or districts, the sheriff principal would compile and maintain a list of suitable persons who would be eligible for appointment as administrator. The Secretary of State should also be empowered to make regulations governing bonds of caution securing the due performance of the administrator's functions; resignation and removal from office; casual vacancies and other incidental matters.

4.228 It should be competent for professional persons (such as accountants or solicitors) to accept office as administrator on condition that they would be remunerated, and their remuneration should be governed by regulations made by the Secretary of State with consent of the Treasury. In such a case, the remuneration would be a prior charge on the debtor's in-payments if a scheme was confirmed. Any unpaid fees not met from that source (e.g. because the scheme terminated early), and the fees incurred in connection with a scheme application which was refused, would be met out of public funds.

4.229 We **recommend:**

(1) The legislation following on this report should provide that sheriff clerks, and their deputes and assistants, should be eligible for appointment as administrator.

(2) It should, however, be competent for the Secretary of State to institute arrangements whereby, throughout Scotland or in particular sheriff court districts, it would be competent for the sheriff to appoint a person from a list compiled by the sheriff principal.

(3) Subordinate legislation should govern such matters as resignation, removal from office, discharge and replacement for any necessary cause and, in the case of administrators who are not sheriff clerks or their assistants, caution and (where the administrator does not consent to act gratuitously) remuneration.

(4) Persons appointed from the list should be entitled to elect either to act gratuitously or to require payment of fees as a condition of acceptance of office. The fees would be a prior charge on payment made by the debtor under a confirmed scheme but to the extent that the fees were not so paid, they should be met by public funds.
(Recommendation 4.31; clause 36.)

Section F. The procedure in scheme applications

4.230 *Regulation of procedure.* In view of the distinctive and novel character of applications for debt arrangement schemes, ("scheme applications"), we have ventured to make full and detailed recommendations as to the relevant procedural rules which we propose should be largely embodied in primary legislation. These rules could be supplemented by procedural rules in an act or acts of sederunt made by the Court of Session under its existing wide powers.[1] We have not thought it necessary to submit detailed recommendations on the procedure in applications for variation or revocation of schemes or for

[1]Sheriff Courts (Scotland) Act 1971, s. 32.

discharge of debts which, we propose, should be regulated by act of sederunt so far as regulation is necessary.

4.231 *Lodging application.* An application for a debt arrangement scheme would be initiated by the debtor lodging in the sheriff court an application in a form prescribed by act of sederunt together with a statement of the debtor's affairs. As recommended later,[1] in relation to all procedures available to a debtor under the legislation following on this report, the sheriff clerk or his depute or assistant would be obliged, on request, to furnish the debtor with information as to the procedure to be followed in a scheme application and to assist the debtor in the completion of the forms of application and statement of affairs.[2] The competent authorities may wish to consider whether the application could be lodged by post or only "across the counter". The application and its relative statement of affairs would have to contain sufficient information to enable the court to check whether the scheme application was competent and could be entertained.

4.232 *Appointment of administrator.* If the application appeared on the face of it to satisfy the conditions of competence, the sheriff would make an order appointing an administrator.

4.233 *Administrator's initial functions.* At the same time as appointing the administrator, the sheriff would pronounce an interim order sisting diligence and the administrator's first duty would be to intimate copies of that interim order to the known creditors. The administrator would interview the debtor with a view to (*a*) assessing the debtor's financial circumstances; (*b*) explaining to the debtor the options open to him in making proposals for payment to his creditors through the medium of a debt arrangement scheme; (*c*) assessing whether any assets could or should be disposed of for payment of debts under the scheme out of the proceeds of sale; and (*d*) assessing generally whether a debt arrangement scheme would be feasible in the circumstances of the case. The order of priority of performing these functions would vary with the circumstances of each case.

4.234 *Statements of the debtor's affairs.* A statement of the debtor's affairs completed by the debtor would be lodged along with his application and at a later stage of the procedure, the same statement, or a fuller statement prepared by the administrator, would be sent to creditors and co-obligants of the debtor entitled to object to the scheme, along with the draft scheme. The statement served on creditors would require to give a full itemised account of the debtor's income, property and liabilities in order to provide the sheriff, the creditors and other interested persons with a full picture of the debtor's financial position as a basis for considering the proposals for payment set out in the draft scheme. It might be found by experience that the statement of affairs lodged with the application should be less full (and therefore perhaps less daunting to applicants for schemes) than the statement circulated to creditors since it would be designed mainly to enable the court and the administrator to check that the financial conditions of competence of schemes

[1]See Recommendation 9.6(1) (para. 9.31).

[2]We also propose that court dues would not be exigible: see Recommendation 9.6(5) (para. 9.31).

were satisfied. The administrator could then elicit from the debtor and other sources the fuller information required for the final statement of affairs circulated to creditors. The contents and form of the statements of affairs should be regulated by act of sederunt, but we suggest that the statement circulated to creditors should disclose the following information:

(*a*) the debtor's name, address and occupation (whether employed, self-employed or unemployed); his or her liability (if any) for dependants (e.g. wife and children supported by debtor and the children's ages), whether alimented in cash or in kind, and particulars of any award of aliment or periodical allowance against or in favour of the debtor;

(*b*) details of any creditors holding a decree for payment which had not been satisfied and information on whether any debt had been or was being enforced by a diligence on the dependence, in security or in execution;

(*c*) details of other debts presently due (including electricity, gas, rent and rates arrears) and of any court action or decree, or any order controlling enforcement under the Consumer Credit Act 1974 relating to those debts; details of any future, contingent or other debt which would be excluded from the scheme;

(*d*) whether the debtor's residence is owned or rented by him; in the case of an owner-occupier, information as to any heritable security; and particulars of any other land or buildings owned or rented by him and of any security;

(*e*) information as to moveable goods, especially goods not likely to be exempt from poinding, owned by the debtor, together with a reasonable estimate of their value; this would cover not only details of any car owned by the debtor but also non-essential household goods together with a reference to any hire purchase or conditional sale agreement affecting the goods;

(*f*) details of co-debtors or guarantors liable along with the debtor;

(*g*) particulars of cash, shares or other savings of the debtor and his or her spouse;

(*h*) information as to the income of the debtor from all sources (the items here varying according as the debtor was employed, unemployed or self-employed) and perhaps also as to the over-all income of the debtor's household;

(*i*) a list of the continuing expenses requiring to be met by the debtor to enable him and his dependants to maintain a reasonable standard of living, including food, clothing, outgoings on the home (rent, secured loan payments, hire purchase or hire payments on necessary goods, rates, house insurance premiums, heating and lighting charges) and also periodic subscriptions to trade unions or professional bodies, and the cost of transport to and from work. The statement should show all the continuing payments which the debtor proposed to make outside a scheme while the scheme was in force.

The statement served on creditors should be accompanied by a declaration

by the debtor that the statement is a full and accurate statement of his financial affairs.[1]

4.235 *Public advertisement for claims.* In our Consultative Memorandum No. 50[2] we suggested that, while the application for a scheme and the interim order appointing the administrator should be available from public court records to the public (e.g. credit rating or reference agencies), in the interests of existing and prospective creditors, advertisement might also be made in the Edinburgh Gazette. No advertisement should be made in the newspapers because the resulting intrusion on privacy and embarrassment might deter debtors from applying for a scheme. On consultation, however, several bodies argued that there should be provision for advertisements inviting creditors to lodge claims, at least in some cases. One body suggested that the normal rule should be advertisement subject to the sheriff's power to dispense with the requirement. Another body suggested advertisement in one newspaper and the Edinburgh Gazette.

4.236 The object of an advertisement would primarily be to ensure that creditors were not erroneously omitted from a debt arrangement scheme. Since a debtor would not obtain a discharge or composition in respect of a debt not inlcuded in a scheme, he would have a strong interest to disclose all debts. As stated above, if a creditor were erroneously omitted, he would have the right to apply for late inclusion or revocation of the scheme or to wait till the termination of the scheme and to enforce his debt in full by diligence. In any event, there is no guarantee that an advertisement would be seen by an omitted creditor. In the circumstances, we propose that, as a general rule there should be no public advertisement in the Edinburgh Gazette or newspapers for creditors' claims, but the sheriff should have power, on the administrator's application, to permit such an advertisement if he were satisfied that there was likely to be an eligible creditor who had not been listed in the statement of affairs or otherwise identified by the administrator. In general, we think that advertisements for claims should be kept to a minimum as an undesirable intrusion on the debtor's privacy, and as a possible deterrent to debtors from applying for debt arrangement schemes. We propose that the cost of the advertisement would be met by the debtor.

4.237 *Verification of debts.* Within a period prescribed by act of sederunt, the administrator should serve on each creditor known to the administrator whose debt was eligible for inclusion in the scheme a notice which would state the amount of the creditor's debt as at "the first notice date" and require the creditor to inform the administrator in writing within 10 days (i) whether he accepted that the amount was correctly stated and, if not, to correct it, and (ii) of any claim for interest on his debt accrued to the first notice date. Failure to comply with the notice would debar the creditor from objecting to the scheme on the ground that the debt or interest was erroneously omitted or stated, unless he could show cause (e.g. that he had not received the notice).

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[1]Any statement false in a material particular made in a statutory declaration is an offence under the False Oaths (Scotland) Act 1933, s. 2.

[2]Para, 2.87.

4.238 **We recommend:**

(1) A scheme application should be initiated by lodging a form prescribed by act of sederunt and a statement of affairs containing particulars also prescribed by act of sederunt.

(2) If the application appears to satisfy the conditions of competence of scheme applications, the sheriff would make an order appointing an administrator.

(3) Within a prescribed period the administrator should require creditors within 10 days to verify their debts and state whether interest accrued before the first notice date was claimed. Failure of a creditor to do so would normally bar him from objecting to the scheme on the ground that the debt or interest was not included or was incorrectly stated in the scheme.

(4) There should be no advertisement for creditors' claims unless ordered by the sheriff. The expenses of any advertisement should be met by the debtor.

(Recommendation 4.32; clause 19.)

4.239 *Protection of creditors' interests.* In seeking to strike a fair balance between the interests of debtors and creditors, we have already recommended important measures to protect creditors, including among other things recommendations that a scheme application, while it was pending, should not prevent the attachment (as opposed to the sale or handing over) of moveable property by poinding or arrestment in common form,[1] nor prevent the inhibition of heritable property transactions,[2] and also recommendations on damages for wrongful diligence, on the recovery of expenses, on second poindings,[3] and on prescription of the debtor's obligations of payment.[4] Further, an application for a scheme would not bar a creditor's application for sequestration if the creditor could show undue prejudice in an application to the sheriff for leave to petition.[5] Other safeguards include powers and duties to refuse a scheme application and undertakings not to remove or dispose of goods, to which we now turn.

4.240 *Powers to refuse scheme application apart from creditors' objections.* In our Consultative Memorandum No. 50, we suggested that the administrator should be entitled to apply to the sheriff for an order dismissing the debtor's application on the ground that the application was not competent or that a debt arrangement scheme would have no reasonable prospect of success.[6] We also suggested a third ground, namely that the debtor had failed to disclose all relevant information or to give assistance reasonably requested by the administrator in connection with the proceedings or had otherwise failed to carry out his duties.

4.241 The proposals were accepted but one body suggested that the third ground should be subject to the qualification that the principal criteria should

[1]Para. 4.109; Recommendation 4.13(3)(*a*)–(*d*).
[2]Para. 4.109; Recommendation 4.13(3)(*f*).
[3]Para. 4.148; Recommendation 4.18(2) to 4.18(4).
[4]Para. 4.216; Recommendation 4.30.
[5]Para. 4.311; Recommendation 4.46(4).
[6]Proposition 9 (para. 2.36).

be the first two and that the third ground should not lead the administrator to apply for dismissal of the proceedings if he took the view that the scheme had a reasonable prospect of success. We accept this qualification since, notwithstanding the debtor's lack of co-operation on a specific matter, the scheme may be feasible and in the best interest of creditors.

4.242 We propose therefore that the sheriff, at any time while the scheme application was pending, should be under a duty to refuse the scheme application if he was satisfied that the debtor was unlikely to comply with a scheme. This would cover cases where the scheme application had been made in bad faith or where for other reasons it was clear that a scheme was not feasible. The sheriff should also have a power (as opposed to a duty) to refuse an application if the debtor had failed to disclose information relevant to the preparation of the scheme or had otherwise failed to co-operate with the administrator. The sheriff would also have a duty to refuse a scheme application if he was satisfied that the conditions of competence were not met, or the financial conditions (the £10,000 limit on indebtedness and the minimum product threshold[1]) were to a substantial extent not met, or that a scheme application, though competent when made, had been superseded by an award of sequestration (competently granted on the petition of a creditor unaware of the scheme application or in pursuance of leave to petition granted by the sheriff under proposals made below) or trust deed for creditors or composition contract.

4.243 On or after refusing a scheme application, the sheriff would recall the interim order sisting diligence. Generally we propose that the sheriff's decisions under the implementing legislation should be appealable, by leave of the sheriff, on questions of law, and we propose that the recall of the interim sist of diligence should not take effect till the expiry of the appeal days or the disposal of any appeal against the refusal of the application.

4.244 We **recommend:**

(1) The sheriff at any time during a scheme application, acting on his own or the administrator's motion without objection by a creditor, should have:

   (*a*) a *duty* to refuse a scheme application if he was satisfied that the conditions of competence were not met, or the financial conditions were to a substantial extent not met, or that the debtor was unlikely to comply with a scheme, or the application was incompetent by reason of sequestration proceedings or a trust deed for creditors or composition contract;

   (*b*) a *power* to refuse a scheme application on the debtor's failure to disclose information to, or to co-operate with, the administrator.

(2) The debtor should have an opportunity to make representations before the sheriff reaches his decision.

(3) On refusing the scheme application, the sheriff should recall the interim order sisting diligence but the recall should not take effect until the expiry of the days of appeal against the refusal of the scheme application

[1]See para. 4.72; Recommendation 4.9(5).

or the disposal of any such appeal.
(Recommendation 4.33; clause 21.)

4.245 *Undertakings not to dispose of or remove property.* Having regard to the relatively limited scope of the restrictions on diligence while an application for a debt arrangement scheme was pending,[1] and to the need to keep the procedure simple, it should not be necessary to confer on the sheriff powers to make interim orders preventing the debtor from voluntarily disposing of his property to the prejudice of creditors, and affecting the rights of third parties transacting with the debtor, pending a scheme application.

4.246 Thus, until a debt arrangement scheme was made, a creditor would be able to register an inhibition in the personal registers, thereby preventing the debtor from granting any voluntary conveyance (including any conveyance in security) of his heritable estate. We considered whether the administrator should be empowered to record in the personal registers a statutory notice of litigiosity having a similar effect to an inhibition, but this would seem to be an unnecessary complication in a procedure which should be kept as simple and inexpensive as possible. The administrator, who would usually be a sheriff clerk, would have to be given a statutory title to raise an action of reduction to enforce the notice at public expense, and special provision would be necessary regulating the duration of the notice including its cancellation if the scheme application were unsuccessful, and as to its possible recall and renewal. On balance, it seems better to rely on the creditors' powers to register inhibitions which would effectively preclude disposal of heritable property.

4.247 Similarly, an interim sist of diligence would not prevent a creditor from laying an arrestment against funds of the debtor in the hands of third parties (e.g. bank accounts) notwithstanding the proceedings for a debt arrangement scheme and this right, together with the right of other creditors holding liquid documents of debt to claim an equal share of the arrested funds under existing legislation[2] would seem to protect creditors adequately without the need for new provisions conferring on the court or administrator special powers to attach funds pending debt arrangement scheme proceedings.

4.248 Not infrequently, the debtor may have property of value which had not been poinded, arrested or affected by an inhibition. Again the scheme may include a condition requiring the debtor to realise property in order to make payment to creditors out of the proceeds of sale.[3] Clearly the debtor should not be entitled to abuse the procedure by disposing of valuable property. We propose therefore that it should be competent for the administrator to require the debtor to give an undertaking not to dispose of specified articles of moveable property pending disposal of the scheme application. On any breach of the undertaking, the sheriff would have a power to refuse the scheme application; a duty of refusal would seem unnecessarily inflexible since the breach might have been inadvertent and the scheme might be in the best interests of creditors notwithstanding the breach.

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[1]See Recommendation 4.13(3) (para. 4.109) above.

[2]Bankruptcy (Scotland) Bill 1984, Sched. 7, para. 10, replacing Bankruptcy (Scotland) Act 1913, s. 10.

[3]See Recommendation 4.4 (para. 4.47).

4.249 We **recommend:**

The administrator should be empowered to require the debtor not to dispose of or remove property from a place in Scotland. The sheriff should have a power to refuse the scheme application if the undertaking was breached. (Recommendation 4.34; clauses 20(6) and 21(3)(*b*).)

4.250 *Power to order valuation of items of property.* We think that the court should possess power to make a remit to a sheriff officer or any other suitable person such as a specialist valuator to make a valuation of items of the debtor's property. Such a power could be useful in deciding whether a provision should be included in a scheme requiring the debtor to dispose of property and pay the proceeds to the administrator for disbursement under the scheme, and might be useful in other circumstances, which we think would be exceptional. We think that the debtor should bear the expense of any valuation.

4.251 We **recommend:**

The sheriff should have power to order a valuation of items of property of the debtor, the cost of which should be borne by the debtor. (Recommendation 4.35; clause 22(3) and (4).)

Preparation and service of draft scheme, and title to object

4.252 On the expiry of the 10-day period for verification of debts and for claims for interest, the administrator would prepare, or complete his preparation of, a draft scheme. To ensure that the scheme would state the debtor's proposals for payment, not what the administrator thought that the debtor should or could pay, the administrator would be required to prepare the draft in consultation with the debtor and, as mentioned above, the debtor would be entitled to withdraw his application at any time. The administrator would also complete his investigation of the debtor's affairs.

4.253 The administrator would serve, on the parties entitled to object to a scheme, a copy of the scheme application and of the draft scheme, a statement of the debtor's affairs (being the statment lodged by the debtor as checked or revised by the administrator or a new statement prepared by the administrator) and also a notice stating that objection may be made to the scheme by notice in writing to the administrator within a prescribed period after the date of service. We think that, as the Law Society of Scotland suggested, three weeks would be an appropriate period, but the period should be variable by act of sederunt in the light of experience.

4.254 To ensure that the procedures were carried through reasonably quickly, the service of the notice giving an opportunity to object should be effected by the administrator within a period prescribed by act of sederunt after his appointment but the sheriff would have power to extend the period on cause shown.

4.255 We propose that the following persons would have a title to object to the scheme, namely:

(*a*) the creditors entitled to be included in the scheme;

(*b*) creditors excluded from the scheme under the rules proposed above who may nevertheless become eligible for inclusion under those rules,

namely creditors in debts which at the first notice date were future; contingent (including co-obligants of the debtor having contingent claims of relief against him); disputed; due under agreements subject to proceedings under the Consumer Credit Act 1974, section 132 or 139; secured by adjudications or contractual securities, or by liens over goods; enforceable by sequestration under the hypothecs or poinding of the ground; or due under hire purchase or conditional sale agreements;

(*c*) co-obligants bound jointly and severally with the debtor even though they may be debarred by contract from ranking in the scheme to recover a claim of relief against the debtor;

(*d*) maintenance creditors not claiming arrears and so not included in the scheme.

The creditors in category (*b*) would have a direct interest in whether a scheme should be made since they would all lose the right to enforce their debts by the ordinary modes of diligence for the duration of the scheme, and they would also have an interest in the terms of the scheme as being potential included creditors. Even "contingent creditors" (who could include persons likely never to become true creditors at all) would have an interest since they would lose the right to seek a warrant for diligence in security, and in some cases the occurrence of the contingency might be probable rather than remote, as where a co-obligant was about to pay the creditor and rank in the scheme by virtue of his right of relief. Probably every co-obligant would have an interest to object to a scheme other than a co-obligant who was severally liable and had no contingent right of relief against the debtor. A co-obligant having a contingent right of relief might be debarred by contract from ranking in the scheme in competition with the creditor but would have an interest to object since, during the currency of the scheme, he would be debarred from enforcing his right of relief by diligence. The scheme would preclude the enforcement of maintenance and recall existing diligences enforcing maintenance though the maintenance creditor had not ranked for arrears. The maintenance creditor would therefore have an interest to object. Accordingly, the draft scheme and other documents would require to be served on all those creditors.

4.256 We **recommend:**

(1) Within a prescribed period, which may be extended by the sheriff on cause shown, the administrator should prepare a draft scheme and serve it on the parties entitled to object to a scheme together with a copy of the scheme application, a full statement of the debtor's affairs so far as known to the administrator, and a notice giving an opportunity to object in writing within three weeks (or other period prescribed by act of sederunt) after service.

(2) The following parties should be entitled to object to a scheme, namely:

(*a*) the included creditors;

(*b*) excluded creditors who may become eligible for inclusion;

(*c*) any co-obligant of the debtor who on paying the debt would acquire a right of relief against the debtor; and

(*d*) maintenance creditors, though not ranking in the scheme for arrears.
(Recommendation 4.36; clause 22(1) and (2).)

Obtaining confirmation of scheme by sheriff

4.257 On consultation,[1] there was general agreement that meetings of creditors should not be called in scheme applications. Such meetings would unduly complicate the procedure and legislation since elaborate provision would be required regulating the calling of meetings, proxies, quorums, adjournments and the like. In the United States, where wage-earners' plans had to be accepted by a majority in number and value of creditors, experience showed that few creditors bothered to attend meetings or even qualified to vote by lodging claims. The U.S. Federal Bankruptcy Commission recommended the abolition of creditors' meetings and argued that an independent determination by the court that a plan met certain statutory standards (e.g. that the wage-earner's plan is in the best interests of creditors and is feasible and the proposal for a plan is in good faith) provided the best protection for creditors.[2] In England and Wales, the grant or refusal of an administration order depends on judicial discretion and the creditors have only a right to be heard.[3] In our Consultative Memorandum No. 50, we suggested certain statutory guidelines or standards,[4] and while there was little dissent by consultees, we think, on reflection, that general guidelines are unnecessary.

4.258 We also suggested that if a majority in number and value of the creditors objected to a draft scheme, the proceedings should be dismissed by the sheriff. The Committee of Scottish Clearing Bankers thought that a majority in value should suffice. On reflection, however, we reject both solutions. A majority in value would require the valuation of securities, and of future, contingent and disputed debts, which we rejected as too complex. Moreover, if debt collection agencies, for example, were to adopt a policy of objecting to schemes on principle, the legislation might become useless.

4.259 If no creditor objected to the scheme within the prescribed period, the sheriff would confirm the scheme. A power to correct any minor error (such as a drafting or arithmetical mistake) without re-service on creditors might be useful. If a creditor did object, the administrator would intimate the objection to the debtor, the other creditors and any co-obligants on whom the application had been served. Having regard to the wide variety of objections which might be made, to require a hearing in every case in which an objection was made would appear to be an unduly rigid rule. An objection might relate to a minor matter which could be resolved without recourse to a full hearing, such as a change in the specified intervals between disbursements or even a small increase in the level of the debtor's in-payments. We suggest

[1]Consultative Memorandum No. 50, para. 2.82.
[2]U.S. Bankruptcy Report, pp. 162–3.
[3]County Courts Act 1984, s. 112. The same solution is adopted in New Zealand for summary instalment orders under the Insolvency Act 1967 (New Zealand) s. 146.
[4]Viz. (*a*) that the scheme has a reasonable prospect of success; (*b*) that the public interest does not require the sequestration of the debtor's estate; and (*c*) that it would otherwise be reasonable to make an order confirming the scheme, having regard to all the circumstances, including the interest of any objecting creditor: Proposition 29(2) (para. 2.84).

therefore a flexible procedure whereby the parties would be given an opportunity to make representations on the objection and only if agreement was not reached as to whether a scheme should be confirmed or as to its terms would a hearing before the sheriff be held.

4.260 At any hearing, we would expect that the sheriff would allow the creditors and any co-obligants concerned or their representatives,[1] to question the debtor as to his financial position and willingness or ability to meet his obligations under the scheme, and also as to any conduct prejudicing creditors which may be alleged or suspected, such as recent gifts to his family or associates, or the granting of unfair preferences, or concealment, disposal or undervaluation of assets, or collusive inclusion in the scheme of fictitious creditors to the prejudice of the real creditors.

4.261 The sheriff should be under a duty to refuse the scheme application if he was satisfied as to the mandatory grounds of refusal mentioned at paragraph 4.244 above. Otherwise, he would have a discretion to confirm the scheme application with or without modifications.[2]

4.262 *Intimation of sheriff's decision.* The sheriff's order confirming a scheme and the scheme itself should be intimated by the administrator to the debtor, and to the parties entitled to object. The order (but not the scheme) should also be intimated to any employer who was operating an earnings arrestment or a current maintenance arrestment against the debtor's earnings since we have proposed[3] that the scheme should render those diligences ineffectual. Where a conjoined arrestment order was being operated by the sheriff clerk of the court in which the order confirming the scheme was made, the sheriff would recall the conjoined arrestment order and that recall would be intimated to the employer.[4] Where a conjoined arrestment order was being operated by the sheriff clerk of a different court, the administrator would intimate the confirmation order to that sheriff clerk, who would arrange for the recall of the conjoined arrestment order and intimation of the recall to the employer.[5]

4.263 Where the sheriff refused the scheme application, he would at the same time recall the interim sist of diligence. The refusal of the application would be intimated by the administrator to the debtor, creditors and any co-obligants who had recived copies of the scheme application and the recall of the interim sist would be intimated to the creditors affected by it.

4.264 The sheriff's decision confirming a scheme should not take effect until the days of appeal (which would be competent on a question of law only) had expired or any appeal taken had been disposed of. Intimation of the confirmation of the scheme to an employer or sheriff clerk operating a diligence against earnings would be effected only after the scheme had taken

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[1]We propose at Recommendation 9:6(2) (para. 9.31) below that provision should be made by act of sederunt allowing lay representation in hearings under the legislation following this report, including applications for debt arrangement schemes.

[2]The modifications could include an extension of the duration of the scheme to be a period of up to five years in all; see Recommendation 4.2(3) (para. 4.41).

[3]Recommendation 4.14(2) (para. 4.118).

[4]See para. 6.266, and Recommendation 6.50(1) and (2) (para. 6.270).

[5]*Idem.*

effect: intimation to other parties would be made forthwith. The interim sist of diligence would be recalled immediately since the order confirming the scheme would itself preclude new diligences while the order is appealable or subject to appeal.[1]

4.265 We **recommend:**

(1) If no objections are made to a scheme, the sheriff should make an order confirming it. It should be competent for him to modify it without re-service on creditors to correct any error in it not materially affecting the interest of any creditor.

(2) Any objection should be intimated to the debtor and the creditors and co-obligants entitled to object who should be given an opportunity to make representations and, failing agreement as to the confirmation or terms of the scheme, an opportunity to be heard.

(3) Following objections or representations by creditors, the sheriff should be under a duty to refuse a scheme application on the same grounds as require him to refuse such an application on his own or the administrator's motion in terms of Recommendation 4.33 (paragraph 4.244) above.

(4) In any other case, the sheriff should have a discretion to confirm the scheme with or without modifications or to refuse the scheme application, subject to the requirement to disregard objections by preferred creditors and creditors wishing to sequestrate proposed at Recommendations 4.11(3) (paragraph 4.96) and 4.46(5) (paragraph 4.311).

(5) An order confirming a scheme or refusing a scheme application should recall the interim sist of diligence.

(6) The administrator should forthwith intimate an order confirming a scheme (together with a copy of the scheme) or an order refusing a scheme application to the debtor, the creditors and co-obligants who received copies of the scheme application. On the coming into force of the scheme, he should also intimate the order confirming the scheme to an employer operating an earnings arrestment or current maintenance arrestment, or to a sheriff clerk operating a conjoined arrestment order in a different court.

(7) An order confirming a scheme or refusing a scheme application, should not take effect until the expiry of the appeal days or the disposal of any appeal, but in the case of an order confirming the scheme, the recall of the interim sist of diligence should take effect immediately. (Recommendation 4.37; clause 24(1)–(4) and (7)–(10).)

Section G. Publication, operation, variation and termination of debt arrangement schemes

4.266 *Publication of debt arrangement schemes.* We propose that public notice of debt arrangement schemes should be given by registration in the register of insolvencies (formerly the Register of Sequestrations), which is a

[1]See Recommendation 4.14(1) (para. 4.118).

public register kept under bankruptcy legislation[1] by the Accountant of Court,[2] but not by advertisements in the newspapers or the Edinburgh Gazette. Further, in each of the sheriff courts, the sheriff clerk should keep a register of schemes which would be open to inspection at all reasonable times by members of the public on payment of a small prescribed fee. The registers would contain particulars prescribed by act of sederunt of discharges of debts and termination of schemes as well as the schemes themselves.[3]

4.267 We **recommend:**

> Prescribed particulars of schemes, discharges of debts and termination of schemes should be registered in the register of insolvencies and by each sheriff clerk in a public register for his own court.
> (Recommendation 4.38; clause 38(1) and (3).)

4.268 *Pay deduction orders ancillary to schemes.* On consultation, there was general agreement with our suggestion[4] that the sheriff should be empowered to make an order requiring payment of a part of the debtor's wages or salary to the administrator for disbursement to the creditors. In Chapter 6 below, we recommend the introduction of new types of earnings arrestment in which the deductions from earnings would be made in accordance with fixed rules in order to avoid the need for a compulsory means enquiry. In the case of a debt arrangement scheme, however, the periodic amounts which the debtor could afford to pay to his creditors would already have been determined on the basis of the debtor's voluntary disclosure of his means and, accordingly, a judicial order for deduction of earnings at source could be made without a compulsory means enquiry. Such a pay deduction order would not be inconsistent with the voluntary character of scheme applications: once a scheme voluntarily applied for had been confirmed, a pay deduction order would give some assurance, however imperfect, to creditors that the debtor would comply with the scheme. The power to make such an order seems essential even though the risk of larger deductions than would be possible under earnings arrestments might deter some debtors from applying for schemes. There are precedents in bankruptcy legislation. In sequestrations under the Bankruptcy (Scotland) Act 1913, the court (on the trustee's application) could grant a declaratory order vesting the bankrupt's after-acquired earnings in the trustee,[5] and though such an order bound the bankrupt rather than the employer, the revised provision in the Bankruptcy (Scotland) Bill 1984 would—it is thought—enable the court directly to require the employer to deduct and remit future earnings.[6]

4.269 We propose therefore that on or after confirming a scheme, the court should have a power, after giving the debtor an opportunity to make representations, to make an order requiring the employer to deduct and pay

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[1]Bankruptcy (Scotland) Bill 1984, clause 1(1)(*c*) replacing Bankruptcy (Scotland) Act 1913, s. 156.

[2]As Accountant in Bankruptcy under the 1984 Bill.

[3]Registration would be a facility for creditors not imputing to them constructive knowledge of schemes; Recommendation 4.18(2)(*b*) (para. 4.148).

[4]Consultative Memorandum No. 50, Proposition 31(2) (para. 2.95).

[5]Bankruptcy (Scotland) Act 1913, s. 98(1); *Caldwell* v. *Hamilton* 1919 S.C. (H.L.) 100.

[6]Bankruptcy (Scotland) Bill 1984, cl. 31(2) and (3); cf. Bankruptcy (Scotland) Act 1913, s. 98(2) construed in *Wilson* v. *Shaw* (1926) 46 Sh.Ct.Reps. 133.

to the administrator the whole or part of the debtor's earnings specified in the order. In some cases, e.g. where the debtor had other sources of income, it may be appropriate to attach the whole of the earnings from a part-time job. The employer should not be liable for failure to comply with the order until seven days had elapsed after intimation.[1] The same fee should be exigible by the employer as we recommend in Chapter 6 in the case of the new diligences against earnings.[2] The order should be subject to variation or recall and should subsist until cessation of employment or until the employer received intimation of recall of the order or termination of the scheme. The order is intended to be a means of securing payments by the debtor to the administrator under the scheme as they fall due; if for some reason (e.g. fluctuation in earnings) a larger amount than the sum currently due was paid by the employer to the administrator, the excess should be paid over to the debtor without delay. The administrator should be entitled to recover from the employer by diligence sums payable under the pay deduction order and the employer's wilful breach of the order would be punishable as a contempt of court without the need for express legislation to that effect.

4.270 We **recommend:**

(1) On or after confirming a scheme, and after giving the debtor an opportunity to make representations, the sheriff should be empowered to make an order requiring an employer of the debtor to deduct and pay to the administrator on each pay day the whole or a specified part of the debtor's earnings until cessation of the employment or intimation of either an order to cease payments or the termination of the scheme.

(2) The employer should have seven days' grace before being required to operate the order.

(3) If the employer does not comply, the administrator should be entitled to obtain an order for the recovery by diligence of the sums which the employer should have deducted and the employer should not be entitled to recover those sums from the debtor.

(4) An employer should be entitled to the same fee on each pay day as an employer operating an earnings arrestment would under Recommendation 6.21 (paragraph 6.125) below.

(5) The administrator should hand over to the debtor any sums paid by the employer in excess of those currently due by the debtor to the administrator under the scheme.

(6) The order should be subject to variation or recall by the sheriff. (Recommendation 4.39; clause 25.)

4.271 *Extent of supervision by administrator.* In our Consultative Memorandum No. 50, we sought views on whether the administrator should be empowered to permit a debtor who had complied with a scheme for a prescribed period to act as his agent in collecting and disbursing moneys due to the creditor.[3] This suggestion, which followed precedents in other countries, was designed to encourage the debtor to budget and manage his own affairs,

[1] See para. 6.97; Recommendation 6.13.
[2] See paras. 6.124 and 6.125; Recommendation 6.21.
[3] Proposition 31(3) (para. 2.95) and para. 2.94.

and to prevent him from becoming dependent on the support and tutelage of the administrator since a primary aim of the legislation is to promote the debtor's financial rehabilitation. However, this proposal was opposed by all who commented, including debt counselling interests, and we therefore reject it. We envisage that the administrator would keep the scheme constantly under review and monitor closely the debtor's in-payments. Given that the administrator would normally be a sheriff clerk or his depute or assistant, it seems unlikely that the administrator could or should have a statutory duty of "money management counselling" or (as in the case of New Zealand supervisors under summary instalment orders[1]) a power of supervising the payment out of earnings of the reasonable living expenses of the debtor and his family. There should, however, be nothing to prevent the administrator from giving informal advice and even encouragement on these matters, and the system would require that a debtor in difficulties should feel free and able to contact the administrator to explain those difficulties.

4.272 *Disclosure of information.* The debtor should be under a duty to disclose to the administrator any material changes in his circumstances occurring during the currency of the scheme. Further, the administrator should be bound to report to an included creditor on the debtor's performance of his obligations under the scheme, if a request for such a report was made by such a creditor. But to prevent the unreasonable repetition of requests by a creditor for reports, the sheriff should have a power to make directions as to whether or when a report should be made.

4.273 *Interdict against disposal or removal of property.* Once a debt arrangement scheme is in operation, it may become clear that the debtor has assets which ought to be made available to creditors whether by diligence or insolvency proceedings but which have been recently acquired or were not disclosed to the administrator. In such a case, it should be possible for the court, on cause shown, to pronounce an interdict prohibiting the debtor from disposing of or removing from Scotland any items of property specified in the interdict in order to protect creditors while, for example, consideration is given to bringing an application for revocation of the scheme or pending such an application.

4.274 **We recommend:**

(1) The debtor should not act as the administrator's agent in making payments to creditors.

(2) The debtor should be bound to disclose a material change in his circumstances to the administrator and subject to any direction by the sheriff, the administrator should, on request, report to creditors on the debtor's compliance with the scheme.

(3) The sheriff should be empowered, on cause shown by the administrator, a creditor or co-obligant, to interdict the debtor from disposing of property or removing property from any place in Scotland.
(Recommendation 4.40; clause 26(1) to (3).)

4.275 *Variation of debt arrangement scheme.* We dealt above with variations

[1]Insolvency Act 1967 (New Zealand), s. 146(9).

of a scheme to include an omitted debt. In addition we think it should be competent for any creditor included in a debt arrangement scheme to apply to the court for variation of the scheme, e.g. for an increase in in-payments and disbursements, where a material change in the debtor's financial position had occurred which might make such a variation reasonable. There may be cases where it comes to light that a debt, or part of a debt, had been wrongly included in a scheme; as where it was accepted as valid by the debtor in good faith and listed in his statement of affairs. On the other hand, where the debtor had listed the debt to give an unfair preference at the expense of other creditors, revocation of the scheme might be the appropriate remedy. The debtor and the included creditors generally (but not omitted creditors) should be entitled to oppose an application for variation by an included or omitted creditor.

4.276 We consider that the court should also have a general power to vary a scheme exercisable, on the debtor's application, not only where there had been a demonstrable change in his financial position (for example, through sickness or unemployment) but also where for example it appeared to the court that the original level of payments had been shown by experience to be unduly high. Most of the comparable systems which we have examined enable the court or administrator to vary the scheme where a debtor is unable to continue payments. For example, in the English administration order system, if at any time it appears to the court that the debtor is unable from any cause to pay any instalment, the court may suspend the order for such time and on such terms as it thinks fit, or vary the amount of instalments.[1]

4.277 The variation of a scheme should not have the effect of reducing the amounts payable under the scheme to any creditor below the amount already disbursed to him, e.g. if the composition was lowered following the inclusion of a debt in the scheme. The sheriff's discretion to confirm a scheme should, in our view, not be controlled by general statutory guidelines, and we think that the same solution should apply to the variation, and indeed the revocation, of a scheme.

4.278 *Subrogation.* A simpler procedure than an application to the sheriff for variation, intimated to all creditors, is required in the case where the only amendment desired is to subrogate a new creditor (such as an assignee, executor or statutory successor[2]) in place of an existing creditor in respect of the whole or part of an included debt. Here we think that the subrogation should be effected by the administrator on an application by the new creditor accompanied by documents (e.g. an assignation or will) deducing title to the included debt. The application would be intimated only to the original creditor (unless he were deceased) and would be granted if the documents disclosed a good title to the debt. An appeal by the applicant or the original creditor to the sheriff should be competent against the administrator's decision in the application.

4.279 We **recommend:**

[1]County Court Rules 1981, Order 39, rule 14.

[2]E.g. the Secretary of State under the Employment Protection (Consolidation) Act 1978, s. 125; see paras. 4.86 and 4.95 above.

(1) The sheriff should have a discretionary power, on cause shown, to vary a scheme on the application of any creditor (included or not), the debtor or the administrator, after giving the debtor and the included creditors an opportunity to make representations.

(2) A variation should not reduce the amount payable to a creditor under the scheme below the sums already disbursed to him under the scheme.

(3) When the right to payment of an included debt is assigned or transmits from the creditor to another person, there should be a simple procedure to enable the administrator to vary the scheme by subrogating the new creditor in place of the original creditor.
(Recommendation 4.41; clauses 27; 28(7) to (9).)

4.280 *Revocation of debt arrangement scheme.* Regrettably, it is likely that a significant number of debtors would default at some point in the life of a scheme because of the high level of self-discipline which compliance with the scheme would require: we understand that the "mortality rate" of English administration orders, New Zealand summary instalment orders and American wage-earner plans is quite high. In considering what default should justify revocation of a scheme, a balance must be struck between the need to prevent a debtor's abuse of the procedures for the purpose of escaping diligence and the need to give the debtor sufficient opportunity to comply with the scheme notwithstanding occasional crises which adversely affect his ability to pay. The proper course for a debtor in difficulties would be to apply for a variation, but he may neglect to do so.

4.281 The administrator would immediately identify default and investigate the reasons for it. We do not propose any system of automatic lapse such as we recommend for time to pay directions and orders (which have no official of the court supervising their operation). The statutory framework should be sufficiently flexible to allow appropriate action to be taken. The creditors and the administrator would have a right to apply for revocation of the scheme or its variation. If it appeared to the administrator that the scheme should be varied (e.g. by a change in the level or frequency of the instalments or temporary suspension of payments), or revoked, he should apply to the sheriff for variation or revocation. The sheriff should have power to revoke the scheme, as an alternative to variation, after giving the parties an opportunity to make representations.

4.282 In our Consultative Memorandum No.50 we suggested, following precedents elsewhere, that specific grounds of revocation other than default should also be prescribed.[1] While we think that revocation on grounds of "misconduct" should be competent quite apart from default, we consider that the administrator and creditors should have a discretion on whether or not to apply to the sheriff where misconduct occurs or the risk of abscondence arises, and that the sheriff should have a discretion to make such order as seems reasonable in the circumstances: though a debtor might have been

[1]Para. 2.110. These were (*a*) that the debtor had given false information to the administrator in his statement of affairs (e.g. particulars of a creditor or debt) or otherwise; (*b*) that the scheme amounted to a fraud on a particular creditor or creditors; (*c*) that the debtor had failed to fulfil his duties under the scheme, or to obey a direction by the administrator or an order of the court; and (*d*) that the debtor had absconded or was likely to abscond or leave the jurisdiction.

temporarily non-co-operative, it might be in the best interests of creditors to continue with the scheme, e.g. if a pay deduction order was operating successfully.

4.283 *Effect of revocation*. We consider that, where a scheme was revoked, it should not necessarily be replaced automatically by the sequestration of the debtor. The expenses of a sequestration might swallow up the debtor's non-exempt assets and it might be to the advantage of the creditors to instruct diligence or for the debtor to grant a trust deed for creditors. On revocation of the scheme, the creditors' rights to enforce their debts in full by diligence or to petition for sequestration would revive and it should be for the individual creditors to choose which course to adopt. Since revocation would have irreversible effects on the rights of parties, we consider that it should not take effect till the expiry of the appeal days or the disposal of any appeal (which under proposals in Chapter 9 would be confined to questions of law).

4.284. *Sanctions against debtor for default or "misconduct"*. The main sanction against a debtor who did not comply with a scheme should be sequestration or renewed diligence. Where the debtor had made a false statement or was guilty of fraud, then he would be liable to prosecution under the False Oaths (Scotland) Act 1933 or at common law. In our Consultative Memorandum No. 50,[1] we sought views on whether on the analogy of the Bankruptcy (Scotland) Act 1913, sections 178 and 179, provision should be made creating specific offences by the debtor or a creditor,[2] but on consultation there was no support for such an approach.

4.285 We **recommend:**

(1) The sheriff should have a discretionary power to revoke a scheme, on the grounds of the debtor's default or misconduct or on other cause shown on application by any creditor, included or not, the debtor or the administrator, and after giving the debtor and included creditors an opportunity to make representations.

(2) On revocation, the unpaid balance of the debts (not merely of the dividend due in a composition scheme) would again become enforceable by diligence.

(3) Revocation should not take effect till expiry of the appeal days or, when an appeal was taken, the disposal of the appeal.
(Recommendation 4.42; clause 30(1), (3), (6) and (7).)

4.286 *Discharge of debts*. Where the debtor had fulfilled all his obligations under the scheme, he should be entitled to obtain a discharge of the debts included in the scheme (apart from special provision for debts included "late" during a scheme and for interest arising after the first notice date). After sufficient payment had been made to the administrator to meet the claims of the included creditors, other than creditors included "late" by variation of the scheme, in full or in the case of a composition to the amount of the composition, the debtor or administrator would apply to the sheriff for a discharge of those

[1]Proposition 33(3), paras. 2.114 and 2.115.

[2]E.g. where the debtor fails to inform the administrator of a false claim, or if he prepares to abscond, or makes a gift of property to defraud creditors; or when a creditor wilfully and with intent to defraud makes a false claim or untrue affidavit or statement.

debts. The application would be intimated to all creditors whose debts were included in the scheme. At the same time, creditors in schemes providing for payment in full would be given an opportunity to claim interest accrued since the first notice date[1] and for this reason the application would be intimated to creditors whose debts had been included but had been satisfied earlier, by payments made outside the scheme, to the extent of their entitlement under the scheme. Before the sheriff decided whether to grant the discharge, the included creditors (but not creditors whose debts had been satisfied earlier) would have an opportunity to make representations, and if agreement was not reached as to whether a discharge should be granted, an opportunity to be heard. We would expect that normally the discharge procedure would be uncontentious.

4.287 In the U.S.A., a debtor may obtain a discharge from debts comprised in a wage-earner's plan where failure to complete the plan was due to circumstances outside his control. This resembles the conditions of discharge under the Bankruptcy (Scotland) Act 1913 where the dividend was less than 25p in the pound;[2] in future under the Bankruptcy (Scotland) Bill 1984, a bankrupt will automatically become entitled to a discharge after three years. In bankruptcy sequestrations, however, the discharge is a *quid pro quo* for the full surrender of assets which a scheme avoids. Having regard to the possibility of variation of the level of in-payments and the extension of the scheme to five years, we think that creditors should be entitled to expect the debtor to comply fully with a scheme. On the other hand, in a five-year scheme, we propose that the sheriff should have power to extend the duration of the scheme by up to three months if it appeared likely that the sums due under the scheme would be paid off within that period, but only one extension of this kind should be permitted. An application for a discharge would have to be made within one month after the expiry of the period for payments under the scheme or such longer period as the sheriff may allow.

4.288 Since a discharge could have irreversible effects, the order for discharge should only take effect after expiry of the appeal days or the disposal of any appeal.

4.289 We **recommend:**

(1) The sheriff should be empowered, on application by the administrator or debtor, to grant a discharge of the debts included in the scheme as originally confirmed where the debtor had paid all the sums required to be paid under the scheme to the administrator in respect of those debts.

(2) An application for discharge should be intimated to creditors whose debts are included, or were included but have since been satisfied to the extent of the creditor's entitlement under the scheme.

(3) The creditors whose debts are included should have an opportunity to make representations and, if agreement was not reached as to whether a discharge should be granted, an opportunity to heard.

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[1]See para. 4.77 and Recommendation 4.10(3) (para. 4.80).

[2]Viz. that the failure to pay the dividend has, in the opinion of the court, arisen from circumstances for which the bankrupt cannot justly be held responsible: 1913 Act, s. 146.

(4) In a five-year scheme, the sheriff should have power to extend the scheme, once only, for a further period not exceeding three months, if it appears likely that the debts would be paid within that period.

(5) The application for discharge should be competent when the debtor's payments under the scheme have been made, but not later than one month, or such longer period as the sheriff may allow, after expiry of the period specified in the scheme for making those payments.

(6) A discharge should not take effect until the expiry of the appeal days or the disposal of any appeal.
(Recommendation 4.43; clause 31(1), (2)(*a*), (4), (5), (11) and (12).)

4.290 *Exceptions from discharge.* We recommended above that in certain cases there should be two types of exception from the discharge of debts in a scheme, namely, claims for interest accruing after the first notice date,[1] and the unpaid balance of the sum due under the scheme to a creditor who had been included "late" by a variation order and who had therefore received fewer disbursements than the creditors originally included in the scheme as confirmed.[2]

4.291 As mentioned above,[3] interest accrued after the first notice date could only be claimed by a creditor in a scheme providing for payment of debts in full, not in a composition scheme. Such a claim could only be allowed in the case of an interest-bearing debt and no separate right to interest would be conferred by the scheme. At the same time as intimating the application for discharge, the administrator would give creditors an opportunity to claim such interest within two weeks (or such other period as might be prescribed by act of sederunt) and to state the amount of interest. The obligation to pay interest which was due but not claimed or allowed would be extinguished if the principal sum bearing the interest was discharged under the scheme. A claim for interest would be intimated by the administrator to the debtor: any dispute as to liability or quantum would be determined by the sheriff in incidental proceedings in the scheme process. If interest was found due, the sheriff would grant a decree for payment of the interest even though interest at a specified rate had been already decerned for in a decree for the principal sum, and the earlier decree would be treated as no longer operative. In such a decree, the sheriff would have a discretion to insert a time to pay direction.

4.292 Since a creditor included late would receive fewer disbursements under a scheme than the original creditors, the sheriff would be under a duty to grant a time to pay decree of the kind described above,[4] for payment of the unpaid balance of the sums due under the scheme, and in the event of default decerning for immediate payment of the balance of the whole debt (not the composition).

4.293 A decree for payment of interest or of the unpaid debt (or composition) would not take effect until the days for appealing against the sheriff's decision

[1]See Recommendation 4.10(3) (para. 4.80).
[2]See Recommendation 4.17(3) (para. 4.143).
[3]Recommendation 4.10(3) (para. 4.80).
[4]Para. 4.142; Recommendation 4.17(3) (para. 4.143).

on interest or discharge of debts had expired or any appeal had been disposed of.

4.294 We **recommend:**

(1)(*a*) In the case of a scheme providing for payment of debts in full, creditors whose debts are included, or were included but have been satisfied to the extent of the creditor's entitlement under the scheme, should have an opportunity to claim interest arising after the first notice date on an interest-bearing debt and to state its amount. The sheriff should determine any dispute as to liability or amount and have power to grant a decree for interest with or without a time to pay direction.

(*b*) A discharge of debts:

(i) in a scheme providing for payment in full, should discharge any interest arising after the first notice date if it is not claimed and allowed by the foregoing procedure;

(ii) in a scheme providing for a composition, should discharge any interest arising after the first notice date.

(2) An order determining a dispute as to interest should not take effect till expiry of the appeal days or disposal of any appeal, and a decree for payment of an unpaid debt such as is proposed at Recommendation 4.10(3) (paragraph 4.80) above, and a decree for interest should only take effect when the discharge or determination takes effect. (Recommendation 4.44; clauses 29 and 31(2)(*b*), (3), (9), (10), (12) and (13).)

4.295 *Termination of scheme.* A scheme would cease to have effect in the following circumstances:

(*a*) revocation by the sheriff's order;

(*b*) the grant of a discharge of the debts included in the scheme as originally confirmed;

(*c*) on the expiry of the one-month period for an application for discharge where either no such application or no application for extending the duration of the scheme had been made or such an application had been refused;

(*d*) on the refusal of an application for variation pending at the end of the one-month period;

(*e*) on the refusal of an application for discharge pending at the end of the one-month period unless the sheriff granted an extension of up to three months as mentioned at Recommendation 4.43(4) (paragraph 4.289); and

(*f*) the debtor's death.

4.296 *Unpaid disbursements.* If for any reason the administrator was unable to make payment of disbursements to a creditor entitled thereto, he should deposit the disbursements in a separate account in a bank authorised to take deposits. At the termination of the scheme, the administrator should send the

deposit receipts to the Accountant of Court who, as we have proposed,[1] should keep a register of subsisting and terminated schemes, and who, in his capacity as Accountant in Bankruptcy, holds deposit receipts for unclaimed dividends in sequestrations.[2] The creditor would be entitled to claim the deposit receipts by application to the Accountant of Court within seven years from the date of termination of the scheme. Any receipts not so claimed at the end of seven years would be handed over to the Secretary of State for Scotland for payment to the Exchequer.[3]

4.297 *Administrator's discharge.* On the termination of a scheme, the administrator would have a number of functions to perform depending on circumstances, such as intimation to the parties of the sheriff's decisions on revocation of the scheme or discharge of debts, intimation of the termination of the scheme to an employer operating a pay deduction order, or deposit of unclaimed disbursements. When these duties had been performed, the administrator would apply to the sheriff for the discharge of his appointment which would be governed by regulations.

4.298 We **recommend:**

(1) A scheme should cease to have effect on the occurrence of any of the events mentioned in paragraph 4.295 above.

(2) There should be a procedure for disposing of unpaid disbursements at the termination of a scheme.

(3) The procedure for discharge of the administrator after termination of a scheme should be governed by regulations made by statutory instrument.
(Recommendation 4.45; clauses 32 and 36(5)(*b*)(i).)

Section H. Debt arrangement schemes, "apparent insolvency", sequestrations and other insolvency proceedings

4.299 Though doubts were raised on consultation by some commentators about the need to regulate the relationship between debt arrangement scheme proceedings and other insolvency proceedings, we believe that, to avoid foreseeable difficulties having to be resolved at the expense of litigants, some provision is desirable, especially (but not only) if, as we now recommend, business debts were to be included in schemes. Other things being equal, the general policy of the law should probably be to foster the use of schemes, at least where a debtor has insufficient assets to make sequestration worthwhile. Other things may often not be equal, however, as when there is uncertainty as to the extent of the debtor's assets, or allegations of unfair preferences or voluntary gifts which a trustee in a sequestration (but not an administrator) would have a title to challenge, or where the creditors include a creditor whose debt would be preferred in a sequestration but not a scheme. Our proposals in Consultative Memorandum No. 50[4] have had to be substantially

[1]Recommendation 4.38 (para. 4.267).
[2]Bankruptcy (Scotland) Bill 1984, clauses 54(1)(*a*) and (*b*), and 55; replacing Bankruptcy (Scotland) Act 1913, s. 153.
[3]Compare 1984 Bill, clause 55.
[4]Paras. 2.18 to 2.20.

revised in the light of the Bankruptcy (Scotland) Bill 1984 without the benefit of consultees' views on some key issues. Our present proposals are as follows.

4.300 First, we propose that the making of the interim order sisting diligence in a debt arrangement scheme should be treated as constituting "apparent insolvency" in the statutory sense[1] for the purpose of clauses in documents (other than unvaried statutory standard conditions in standard securities over land[2]) such as clauses providing for termination of the contract, or acceleration of payments or repossession of goods e.g. held on hire purchase or hire. Since the coming into force of a scheme would prevent a creditor from constituting apparent insolvency by service of a charge, and would cause an unexpired charge to lapse, a creditor might lose the benefit of the clause in the absence of such a provision. Moreover, a scheme application is an acknowledgment by the debtor of practical insolvency. We have hesitated to go further and propose that the interim order should have all the effects of apparent insolvency, such as the equalisation of diligences,[3] or the various enactments imposing disqualifications on persons who are notour bankrupt or apparently insolvent from public office, membership of statutory authorities, or holding of various licences,[4] though we suggest below[5] that it should enable a creditor to petition for sequestration. Such a proposal might be considered a logical extension of out recommendations and we would not oppose it.

4.301 Second, we propose that, as a general rule, a scheme application should not be competent while a petition for sequestration of the debtor's estate was continuing or sequestration had been awarded but the debtor had not obtained his discharge. We propose that this rule should apply even where the scheme application and the sequestration involved different creditors, as where an undischarged bankrupt sought to obtain a debt arrangement scheme relating to debts incurred after the award of sequestration, as a protection against the diligences of post-sequestration creditors (whose claims would not be admissible in the sequestration). The trustee in the sequestration would be entitled to obtain an order attaching the undischarged bankrupt's personal earnings so far as exceeding a suitable aliment[6] and we agree with the comments of the Law Society of Scotland that those earnings should not be subject to a debt arrangement scheme.

4.302 We think that a subsisting trust deed for creditors or composition contract should have the same effect as a sequestration in precluding a scheme application, but, with the repeal of section 14 of the Bankruptcy (Scotland) Act 1913.[7] it seems unnecessary to make comparable provision with respect

[1]Bankruptcy (Scotland) Bill 1984, clause 7.

[2]See Recommendation 4.23(3) (para. 4.174).

[3]Bankruptcy (Scotland) Bill 1984, Sched. 7, para. 10, replacing Bankruptcy (Scotland) Act 1913, s. 10.

[4]See para. 4.312 below.

[5]Para. 4.302.

[6]Bankruptcy (Scotland) Bill 1984, clause 31(2) and (3).

[7]This section empowered the court to appoint a judicial factor for the immediate preservation of an estate which was the subject of a petition for sequestration. Judicial factories under the 1913 Act, s. 163 (replaced by Judicial Factors Act 1889, s. 11A as set out in the Bankruptcy (Scotland) Bill 1984, Sched. 7) relate to deceased debtors, and judicial factories on bankrupt estates of living debtors will be competent only under the residual common law powers of the court.

to judicial factories on bankrupts' estates, which are likely to be unusual in the case of living bankrupts. Nor do we think it necessary to make express provision regulating competitions between on the one hand debt arrangement schemes and, on the other, English adjudications in bankruptcy or administration orders under the County Courts Acts or other insolvency proceedings outside Scotland.

4.303 Third, there does not seem to be much scope for a special procedure enabling a sequestration to be replaced by a debt arrangement scheme. Already there are provisions enabling the creditors in a sequestration to accept an offer of a composition by the debtor. Generally the offer must be of at least 25p in the pound, secured by caution or other security,[1] and be accepted by a majority in number and not less than two-thirds in value of the creditors.[2] Such judicial composition contracts are unusual but some of the former procedural restrictions are relaxed by the Bankruptcy (Scotland) Bill 1984, and we think that rather than provide for a change from sequestration to a scheme, it might be more appropriate to relax the requirements of judicial composition contracts in cases where the total indebtedness does not exceed the financial limit for schemes. We identified this option late in our consideration of schemes, have not consulted on it, and make no firm recommendations but, if schemes are introduced in Scots law, consideration might be given to relaxing the requirements of judicial composition contracts in cases which would be eligible for a scheme if there had been no sequestration.

4.304 Fourth, while we do not propose that proceedings in a scheme application should have the effect of constituting "apparent insolvency" (except for the purpose of clauses in deeds and contracts[3]), we think that in an important respect the appointment of an administrator should have effects similar to apparent insolvency[4] insofar as it should enable a qualified creditor or creditors to petition for the debtor's sequestration. Normally, a debtor will already have been rendered "apparently insolvent" with the service of a charge prior to the scheme application, but the scheme application may have been "triggered" by an arrestment in common form which does not create apparent insolvency.[5] A scheme application would imply practical insolvency and we think a creditor should not be put to the delay and pointless expense (for which the debtor would be ultimately liable) involved in serving a charge.

4.305 Fifth, there ought however to be some restraint on a creditor's right to supersede a scheme application by a petition for sequestration lest that right be exercised unreasonably. We propose that any creditor on whom an interim order sisting diligence has been served, and who has therefore official notice of the scheme application, should apply to the sheriff for leave before presenting a petition for sequestration. On the model of the tests which the courts will apply in determining whether a sequestration should be permitted to supersede a "protected" trust deed for creditors,[6] the sheriff should grant leave to petition only if it appeared to him that sequestration would be likely

[1]Bankruptcy (Scotland) Bill 1984, Sched. 4, para. 3.
[2]*Ibid.*, para. 8.
[3]See para. 4.300.
[4]Bankruptcy (Scotland) Bill 1984, clause 5(2)(*b*).
[5]*Ibid.*, clause 7.
[6]*Ibid.*, Sched. 5, para. 7.

to be in the best interests of the general body of creditors or that a scheme would be unduly prejudicial to a particular creditor or class of creditors. On granting leave, the sheriff should sist the scheme application to allow the petition for sequestration to proceed. If sequestration was not awarded, he should recall the sist and the order granting leave to petition, and make such consequential orders as might be necessary to allow the scheme application to proceed. If an award of sequestration were made, the sheriff should refuse the scheme application on his own or the administrator's motion.

4.306 Sixth, we think that if a creditor did not petition for sequestration (with the sheriff's leave) prior to confirmation of the scheme, he should not be entitled to oppose a scheme application on the ground that he wished to petition for sequestration. If a scheme application were refused on that ground, there would be no assurance that the creditor would in fact petition for sequestration. Moreover, we have already proposed[1] that a creditor should not be entitled to oppose a scheme application on the ground that he would not obtain a preference in a scheme which he would have obtained in a sequestration.

4.307 Seventh, once a scheme had been confirmed, it should not be competent for any creditor, whether included or not, to present a petition for the debtor's sequestration while the scheme subsisted. The creditor should be entitled to apply for revocation of a scheme which the sheriff would have a discretion to grant or refuse having regard to all the relevant circumstances including the length of time which the scheme had yet to run. In exercising his discretion, however, the sheriff should be required to disregard an argument to the effect that the creditor was being deprived of a preference which he could obtain if the scheme was revoked with the result that he would then be able to sequestrate.

4.308 The effect of the proposals in the preceding paragraphs would be that a creditor having a preference in a sequestration or who desired to sequestrate for some other reason would have to act timeously by petitioning for sequestration (with the sheriff's leave); and could not found on that preference or his desire to sequestrate as a ground for objecting to or for revoking a scheme.

4.309 Concurrent debt arrangement scheme proceedings are most unlikely to occur given that only the debtor can apply for a scheme. For completeness, however, it should be made clear that a scheme application would be incompetent if a scheme was already in force, or if a scheme application had been previously commenced and was still pending.

4.310 We think that provision should be made by act of sederunt to secure that the debtor would include in his scheme application a statement that to the best of his knowledge and belief no sequestration proceedings were continuing in the same or another court, and also a statement in unqualified terms that no trust deed for creditors, composition contract, scheme application or scheme was subsisting.

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[1]Recommendation 4.11(3) (para. 4.96).

4.311 We **recommend:**

(1) The making of the interim order sisting diligence in a scheme application should be treated as constituting "apparent insolvency" in the statutory sense for the purpose of clauses in legal documents (other than statutory standard conditions in standard securities).

(2) A scheme application should not be competent if:

(*a*) at the time of the scheme application:

(i) a petition for sequestration of the debtor's estate was pending, or sequestration had been awarded but the debtor had not yet obtained his discharge; or

(ii) a trust deed for creditors or composition contract was subsisting; or

(iii) a scheme was already in force or a prior scheme application by the debtor was pending; or

(*b*) during the scheme application sequestration is awarded or a trust deed for creditors is granted or a composition contract is made.

(3) A qualified creditor petitioning for the debtor's sequestration at any time between the intimation to the creditor of an interim order sisting diligence and the disposal of the scheme application, should not be required to establish that the debtor was "apparently insolvent" in the statutory sense.

(4) (*a*) While a scheme application is pending, a creditor should not be entitled to present a petition for the debtor's sequestration unless he has obtained the leave of the sheriff having jurisdiction in the scheme application.

(*b*) Leave should be granted only if it appears to the sheriff that sequestration would be in the best interests of the general body of creditors, or that the scheme would be unduly prejudicial to a particular creditor or class of creditors.

(*c*) There should be procedures for sisting the scheme application to allow a petition for sequestration to be presented; for recalling the sist and restarting the procedure if sequestration is not awarded; and for refusing the scheme application if sequestration is awarded.

(5) A creditor should not be entitled to oppose a scheme application on the ground that he wished to petition for sequestration.

(6) A petition for sequestration should not be competent while a scheme is in force, without prejudice to a creditor's right to apply for revocation of a scheme, and to petition for sequestration if the scheme is revoked.

(7) An act of sederunt should require an applicant for a scheme to state in his application that no trust deed for creditors, composition contract, scheme, or scheme application was subsisting, nor to his knowledge any petition for or award of sequestration was subsisting.
(Recommendation 4.46; clauses 17(2); 18(1)(*c*); 20(4); 21(2)(*d*), (*e*) and (*f*); 24(4)(*a*)(iv), (v) and (vi); 24(5); and 35.)

4.312 *Bankruptcy disqualifications.* A large number of specific enactments place insolvent persons under certain civic disqualifications or disabilities, or

render them liable to be disqualified from statutory office by the act of a government minister. While these enactments normally link the disqualification to sequestration, the enactments disclose no coherent or consistent policy towards other states of bankruptcy or insolvency processes recognised by law. For example, sequestration alone disqualifies a person from sitting or voting in the House of Lords or House of Commons,[1] from membership of a local authority,[2] from acting as a J.P.,[3] or as director[4] or receiver[5] of a company, or from holding a licence to conduct a credit or hire business.[6] A solicitor is liable to suspension from practice not only if he is sequestrated but also if he grants a trust deed for creditors.[7] In the case of membership of statutory boards, disqualification seems normally to be linked to sequestration, a trust deed for creditors or a composition contract,[8] but in some cases notour bankruptcy is in effect added,[9] in other cases a composition contract is not a disqualification,[10] and in other cases simple bankruptcy or an arrangement with creditors suffices.[11]

4.313 Against this background we think that a debtor who has applied for or obtained a debt arrangement scheme should not be subjected to civic disabilities. To make a debtor subject to such disqualifications might discourage debtors from applying for schemes which might be in the interests of creditors as well as themselves. So far as we are aware, an administration order under the County Courts Acts in England does not attract civic disabilities. This proposal was generally accepted on consultation.

4.314 We **recommend:**

The disqualifications from public office applying to an undischarged bankrupt should not be extended to a debtor who has applied for or obtained a debt arrangement scheme.

(Recommendation 4.47; Schedule 7, paragraph 39.)

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[1]Bankruptcy Act 1883, s. 32, as read with Bankruptcy (Scotland) Act 1913, s. 183, replaced by Bankruptcy (Scotland) Bill 1984, Sched. 7, para. 11(*a*).

[2]Local Government (Scotland) Act 1973, s. 31(1)(*b*).

[3]1883 Act, s. 32 (*supra*).

[4]Companies Act 1985, s. 302 (leave of the court is required).

[5]*Ibid.*, s. 467(3).

[6]Consumer Credit Act 1974, ss. 37 and 38.

[7]Solicitors (Scotland) Act 1980, ss. 18(1); 15(2)(*h*).

[8]E.g. membership of the electricity boards, the Countryside Commission, Nature Conservancy Council, Highlands and Islands Development Board, Tourist Board, Scottish Development Agency, Civil Aviation Authority: see e.g. Electricity (Scotland) Act 1979, Sched. 1, para. 2; Countryside (Scotland) Act 1967, Sched. 1, para. 2(3).

[9]Sex Discrimination Act 1975, Sched. 3, paras. 3(5)(*b*) and 7(5)(*b*); Race Relations Act 1976, Sched. 1, paras. 3(5)(*b*) and 7(5)(*b*).

[10]Teaching Council (Scotland) Act 1965, Sched. 1, para. 4(2) (sequestration or trust deed).

[11]New Towns (Scotland) Act 1968, Sched. 2, para. 5 (membership of development corporation).