

Response to call for further evidence in paras 85 – 87 of the Stage 1 Report of the Delegated Powers and Law Reform Committee on the Moveable Transactions (Scotland) Bill

Dear Sir

I have been encouraged to write to you directly by Hamish Goodall of the Civil Law and Legal System Division. I was an original, and am a continuing, member of the Scottish Law Commission working party on the report which has led to the introduction of the Bill and, along with others on that working party, have been regularly assisting that Division on technical issues arising with the contents of the Bill.

I retired last year as a practising solicitor; until that retirement I was recognised as a leading practitioner in the fields of invoice finance and asset finance, acting mostly for finance companies. These are the two fields of the finance industry most concerned with the Bill and, in particular, with the need for the reforms, which are the subject of the Bill, because of the disadvantages the Scottish economy faces under the existing, old-fashioned Scottish legal rules. I am the author of the Scottish section of *Salinger on Factoring*, the current, and only, UK legal textbook on invoice finance – in other words, on that part of the finance industry which finances businesses by buying their debts or invoices.

I wrote previously to the Committee, prior to the publication of your Report, expressing concerns, along with the others on that working party, that many of the recent responses to your committee's consultation from consumer debt advisers misunderstand the current practical situation, the legal position in England to which they make reference, and the consequences of the Bill.

The Committee's attention now, though, in seeking further responses in paragraphs 85-87 of your Report, is restricted to the issue of any risks to consumers arising from dispensing with the need for intimation or notice of the assignation of a consumer debt from one creditor to another. I shall, therefore, deal only with that issue in this response. If the Committee wishes me to revisit the wider issues dealt with in my previous response, please let me know.

Quite simply, the concerns expressed in the responses to the Committee prior to its issue of its Report (see the paragraphs preceding paragraph 85 of the Report) are misconceived and based on a misunderstanding of current legal and financial practice. To put it another way; these concerns while expressed with the best of intentions and a wholly understandable concern for the position of indebted consumers are, in common parlance, a red herring. Consumer debt owed by Scottish consumers to business lenders is currently routinely and day and daily transferred from one creditor to another without intimation or notice being given to the consumer, without any detriment to the consumer. The problem with the current law, therefore, is not that there is no alternative to the giving of intimation or notice following assignation but rather that the workaround which has been devised is clunky, time-consuming to put in place and thus expensive (as detailed legal advice

is always required). Scotland is thus out of step with all other developed economies in the workaround and legal expense required (and thus the finance cost incurred).

I shall explain how this works in practice and then why there is no detriment to consumers. The fact that all that follows goes on behind the scenes, as it were, explains why those expressing the concerns referred to above have no visibility of it.

Non-notification to the debtor of the assignation of a debt by one creditor to another

The simple fact is that consumer debts are currently being assigned in Scotland day and daily from one creditor to another (the assigning creditor's funder) without notice being given to the debtor. Of course, we are not talking here of the assignation of a debt in a private non-business transaction. Rather we are talking of the everyday invoice finance transaction where a business obtains its funding from a funder through the sale of its debtor book to that funder. Another example is where a credit card provider transfers a portfolio of the credit card indebtedness, as currently due to it by its credit card holders, to another lender. The legal agreements used to achieve this are unnecessarily complex in Scotland (and only in Scotland) which is one of the critical reasons for the reform. I can go into considerable detail if required as to how this transfer without notice to the consumer debtors is safely achieved so far as the assignee or buying creditor is concerned but will content myself here with the briefest of explanations. The key workaround is the use of a trust device. The creditor assigning (i.e., selling) the portfolio of consumer debts enters into a declaration of trust each time the debts are sold, declaring that it has sold the debts, received the purchase price of the portfolio and that it now holds title to those debts on trust for the purchasing assignee creditor. This trust puts the assets bought by the purchasing assignee creditor out of the reach of any creditors of the assigning selling creditor, in whose estate if insolvent the benefit of the debts is replaced by the purchase price received. The legal expense and the caution with which such transactions are approached results not only from the need for the creation of the trust but also from difficult legal questions about what needs put in place to ensure the efficacy of the trust mechanism.

The key point for today's purposes, however, is that in current practice there is no need for the consumer debtor ever to learn of the transfer, because the collection of the debt and the payee of the debt so far as the consumer is concerned never changes. The usual arrangement is that the original creditor carries on collecting the debt and dealing with the consumer debtor, but now undisclosed on behalf of the assignee. If, for any reason, the assignee needs to step in (and terminate the collection authority of the original creditor) then of course it needs to notify the consumer debtor that the debt has been assigned and payment should be made to it. It is only at that point, should it ever occur, that notice of the assignation need be given to the debtor.

Protection of the Consumer Debtor who is unaware of an Assignation

The Bill protects a debtor who innocently pays the original creditor, not having received notice of the assignation to the assignee. This is a key protection in the Bill (and is also the current law in relation to any assignation of a debt). If a debtor,

consumer or otherwise, pays his original creditor when having no valid notice of an assignation to a subsequent creditor, his debt is discharged.

Apart from the foregoing protection for the consumer debtor paying the wrong creditor innocently, there is a further key issue which has been ignored in the responses received the Committee prior to its Report. This issue is consumer protection legislation enshrined in the Consumer Credit Act, Financial Services and Markets Act and the remit of the Financial Conduct Authority (FCA). It lies behind the methodology outlined above. A business which collects consumer debt where it is not the original lender can only do so if approved and authorised to do so by the FCA. The authorised business collecting consumer debt must do so in accordance with the FCA's rules protecting consumers. Thus, if an assignee purchasing creditor of a consumer debt is not so approved and authorised, it must leave the collection in the hands of the assigning, original creditor as outlined above or, alternatively, appoint another authorised person to do so and notice must then be given to the debtor in the ordinary way that the debt has been assigned and payment should be made to the new FCA authorised collector. Of course, if the purchasing assignee creditor is in fact itself authorised by the FCA to collect consumer debt, then it has the choice of leaving collection and administration of the debts in the hands of the original assigning creditor or, alternatively, giving notice in the usual way to the debtor that the debt has been assigned and then collecting and administering the debts itself.

None of this changes with the abolition of the need for notice in the Bill. A purchasing assignee creditor will either employ the selling assigning creditor to continue to collect the debts or will give notice and collect the debts itself (if the purchasing creditor is FCA authorised) or will employ a new collecting agent to do so (if it is not). The benefit of and need for the Bill lies entirely outside the issue of the protection of the consumer. It is twofold: the simplifying of the complex legal process which must currently be used to effect the assignation using the trust mechanism; and the simplifying of ancient legal rules as to how notice is given, which simplification is designed to help make sure the consumer debtor understands what is going on and what is required of him in situations where notice needs to be given.

I hope this is helpful to the Committee in informing your deliberations. I am at your disposal to discuss with the Committee any of the above and, as required, to give more detail.

Yours faithfully

R Bruce Wood CVO, WS
Member of the Scottish Law Commission working party on the Moveable
Transactions Bill