

Doing Business in the Isle of Man

Thursday November 15 2012

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Manx society faces reduced state role

Andrew Bounds finds a model of European welfare combined with low taxes being re-examined as revenues fall and slowdown hits the banks

At first glance little seems to have changed on the Isle of Man. It has just posted its 28th year of economic growth, the bars of Douglas team with suited bankers and lawyers and horses still pull trams along its seafront during the summer season.

Yet it is facing its toughest test since its offshore financial sector was established in the 1980s in response to a deep recession.

Its model of European welfare combined with low taxes is being re-examined as revenues fall and the global slowdown hits its banking sector.

Once unheard of, industrial strife is growing: state-employed bus drivers have been dismissed for refusing to accept the loss of paid lunchbreaks, while civil servants grumble about redundancies and curbs on their pensions.

Allan Bell, the experienced former treasury minister who now heads the government as chief minister, has drawn up an “agenda for change” setting out a smaller state and fewer benefits while maintaining the “cohesion of Manx society”.

He says the economic change – chiefly driven by the UK revising an agreement in 2009 on how to share value added tax revenue, which slashed government finances by about a third – represents an “opportunity and a challenge”.

“The Isle of Man is starting from a position of strength. We have avoided recession and unemployment is still low,” he says. Gross domestic product per head is higher than in the UK.

But with the UK economy sluggish, the euro crisis spreading uncertainty, and regulatory pressure increasing, “we have to be swifter in identifying new niche opportunities for the future to enable us to continue the growth we have enjoyed now for 28 years”.

As a self-governing dependency of the British Crown, the 81,000 strong island has not hesitated to adjust its laws to attract business.

It is an important operator in the space industry, with one in four satellites launched last year being owned on the island. It retains a strong manufacturing industry, especially in

aerospace, nurtured by government support.

It has also created successful ship and aircraft registries, which bring business to the island’s professional communities by arranging mortgages and companies to own the assets.

The attraction of an online gaming cluster has blessed it with impressive IT infrastructure. It invested in the good times in plentiful power and road infrastructure, which could be augmented by offshore wind farms in the Irish Sea.

Nevertheless, Standard & Poor’s, the rating agency, downgraded its AAA credit rating a notch in November 2011, citing external factors. It retains a AAA rating from Moody’s.

Mr Bell says: “We have to recognise government cannot provide everything in the way it has in the past and, if we are going to maintain a competitive tax structure... there have to be limits. Tax increases would be totally counterproductive.”

That requires means testing child benefit and squeezing some savings reliefs to bring the budget

Once unheard of, industrial strife is growing, with bus drivers sacked and civil servants grumbling about redundancies

into balance by 2015-16.

Nevertheless, the island has a stronger revenue base than many offshore jurisdictions because of its 20 per cent VAT rate shared with the UK. It also attracts companies that can register for VAT there and trade in the European Union.

The top rate of income tax is 20 per cent and there is no inheritance tax, stamp duty or capital gains. Banks are the only businesses subject to tax, at 10 per cent.

Mr Bell says that, while the island would continue to comply with relevant international tax and money laundering agreements, there was “an

air of hypocrisy” about some British rhetoric.

The UK government has attacked the behaviour of offshore centres while encouraging French investors to flee high taxes there and crowing about reductions in corporate tax luring back multinationals.

However, he says the relationship with the UK had “calmed down a bit” since the revenue sharing changes.

“We need to protect the economy,” says Mr Bell. “We are anxious to see a level playing field. You look to Asia and see Singapore and Hong Kong and other emerging centres and question whether they are following the same standards. I still have to be convinced that the regulatory pressures are applied equally to competitors.”

As part of its diversification the island’s government in October took a 9.99 per cent stake in Pinewood Shepperton, the film studios, and gave Pinewood access to £25m of public money to invest in films. Filming would be done at the studios and on the island. Pinewood is owned by John Whittaker, the billionaire chairman of Peel Holdings, the property, media and logistics group, who lives on the island and discussed the deal directly with Mr Bell.

Peter Karan, a minister who was sacked for voting against the Pinewood deal, says he fears that government plans for outsourcing or “corporatising” services to cut costs could reinforce a too-cosy relationship between the government and business. “It is a system built on patronage,” he says. His Liberal Vannin party is calling for an inquiry into the Pinewood deal.

However, Mr Bell wants to make more use of the wealthy on the island. Teaming up with Peel Holdings in other areas would enable it to funnel overseas investment to northwest England and show that the island “is a genuine partner for good, not a tax haven on a sandspit in the Irish Sea”, he says.

Despite the commitment on tax, an increase from 18 to 20 per cent in 2010 has made business leaders nervous. Garth Kimber, chief executive of Xela Holdings, an online gaming company,



Headwinds: the island is facing its toughest test since the 1880s

Alamy

says: “Maintaining zero corporate tax is vital. It has got to be a government strategy. They have made all the right noises but, until you see that [budget] gap closed, there is a degree of concern. I would like to feel 100 per cent certain. It is an island and not everybody wants to live on an island. If we want to bring quality employees over, they have got to see the benefits.”

There are also worries about access. Mr Bell admits that he has concerns over a proposed offshore wind farm in British waters that could interfere with the vital Steam Packet ferry service from Liverpool and Heysham. “We can’t afford any disruption to the sea links. It is the lifeline for the island. For our business community and for manufacturing in particular,” he says.

Noel Hayes, chairman of Manx2.com, which charts regular flights to unscheduled destinations such as Gloucester and Belfast, says

he is worried that its air links could be reduced.

Easyjet has begun services from Liverpool, using large 150-180 seat aircraft, while Flybe has the biggest network, using 80-seat aircraft. Easyjet is offering cheap new capacity he says but, with 700,000 passengers a year, bigger aircraft could mean fewer flights.

“The island can have economy or frequency,” he says.

He welcomed a review announced on the open skies policy, citing the example of Guernsey, which still controls access to its airport to ensure operators can make money and provide frequent flights.

Nevertheless, most businesses remain committed to the island. Bill Mummery, executive director of Celson Manx, an egaming company, quotes the latest marketing slogan: “The Isle of Man, where you can”. It does what it says on the tin.”

Lights, camera but slightly less action

Film

Andrew Bounds finds the industry’s attractions are being outmatched by rivals

The Isle of Man may be small but it is adaptable. It has featured as the slums of Victorian Bristol, the rolling hills of Ireland, the rugged coast of Cornwall and even urban locations such as Boston and Hamburg in some of the 100 films shot there since 1995.

Stars such as Johnny Depp (*The Libertine*) and Claire Danes (*Me and Orson Welles*) have set foot on the island, bringing a touch of glamour – and much needed spending in its restaurants and hotels offshore.

The first film was *The Brylcreem Boys*, the 100th was *Dom Hemingway*, a gangster film with Jude Law and Richard E. Grant, that is still in production.

According to a report by Oxford Economics, the consultancy commissioned by the government, the film industry brought £81m in benefits and created 2,140 full-time equivalent job years.

The government has invested £170m (in 2011 prices), which has generated £85m from producers through the equity share of revenues and £375m from

additional tax revenues.

However, changes to value added tax rules that put an end to the island keeping the VAT earned on cinema screenings in the UK have hit the industry hard.

The UK and Ireland then extended their own tax breaks. It costs about £250,000 extra to make a production on the island. From a high of 12 in 1997, only two productions were made there in 2011. The number of days of filming has fallen from 830 in 1997 to 25 in 2011.

“The competitive offer of the Isle of Man to film producers is now relatively poor compared to its competitors, lagging both the UK and Ireland in terms of tax incentives, local cost structures, skills and the variety of image locations for film making,” Oxford Economics concluded. “Not only is the Isle of Man relatively uncompetitive when it comes to attracting filmmakers, it is also operating in a declining market.”

Hilary Dugdale, who runs the government’s film unit, Isle of Man Film, says the government’s proactive help, such as closing roads and providing equity funding, was no longer sufficient to entice filmmakers. She says it is important to bring in the spending of film crews, which also provided temporary jobs for many on the island and that change is needed.

However, the path chosen has caused controversy, with seven members of Tynwald, the parliament, voting against and one minister being sacked for doing so in June. The government decided to take a stake in Pinewood Shepperton, the famous studios near London where James Bond movies are made, and allow it to use £25m of its publicly funded Media Development Fund (MDF) to invest in films. This gives Pinewood the ability to create demand for its studios, while many outdoor locations would be on the island. The plan to take a 9.99 per cent stake was reduced to 9.99 per cent and purchased for £12.2m at the end of October.

Pinewood was bought a year ago by John Whittaker, the billionaire chairman of Peel Holdings, the property, media and logistics group, who lives on the Isle of Man.

In 2007 management of the MDF was handed to CinemaNX, a Manx company, to run. Steve Christian, the co-founder of CinemaNX, has taken a board seat at Pinewood and four staff have transferred to the studios.

Mr Christian and Ivan Dunleavy, Pinewood Shepperton chief executive, have joined Prosper Capital which is already licensed by the Financial Services Authority, as well as registering Pinewood Film Advisers with the FSA.



On location: *Dom Hemingway*, currently in production and starring Jude Law and Richard E. Grant, was filmed partly on the island

Closing roads and providing equity funding is no longer sufficient to entice filmmakers

Asia internet gaming on a roll

Gambling

Andrew Bounds reports on a new revenue source that accounts for almost 10 per cent of GDP

Away from the Victorian terraces of the lawyers and bankers in downtown Douglas is a glimpse of the future for the Isle of Man.

On the edge of an industrial estate stands a modern edifice clad in local stone with huge floor-to-ceiling windows. It is Celson Manx House, the new home of the Asian company behind the SBOBet internet gaming brand.

Bill Mummery, executive director of Celson Manx, says it is a statement of his business’ commitment to the island. His corner office, lined with prints of the island, commendations for the group’s charity work and photographs of Mr Mummery’s encounters with the sporting elite – SBOBet sponsors West Ham United and the Manx national football team, for example.

“Celson came here in 2005 because it wanted a quality jurisdiction. You have the English legal system, regulation specific to the industry and, as most of our markets are outside the EU, we pay VAT only on the revenue we generate in the EU,”

he says. “Since then, the challenge has been managing growth.”

The island is on the UK’s white list, allowing licence holders there to serve UK punters. Celson’s main operations are in the Philippines, where it runs live casinos for its website and its customer service teams.

But the Isle of Man has huge data storage centres that are not vulnerable to typhoons, vast broadband and satellite communications capacity and the banking facilities to handle clients’ money.

Hence egaming, one of the island’s newest industries, is one of its fastest growing. From a standing start a decade ago it now accounts, with information technology, for about 9.7 per cent of gross domestic product.

As well as Celson, 188Bet is headquartered on the island, Paddy Power has a base there, along with software companies enabling the online growth, such as Playtech and Microgaming.

There are not, however, huge numbers of jobs (about 750), admits Tim Crane, the government’s egaming ambassador, but they are well paid. “It has been a very important contributor to our economy.”

It also provides the demand to justify investment in data centres and telecoms infrastructure that helps all businesses. Licenses pay £35,000 plus 1.5 per

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Doing Business in the Isle of Man

Plan to win customers in emerging markets

Financial services Government strategists are developing country-by-country approach to promotion of specialist skills, writes *Brian Groom*

Financial services remain the bedrock of the Isle of Man's economy, despite the island's successful push to diversify into areas such as e-gaming, manufacturing and information technology.

The financial sector makes up 35 per cent of gross domestic product and employs a quarter of the working population. Its share of GDP has fallen from 48 per cent in 2001 as other parts of the economy have expanded, but it still contributes to growth. Life assurance is the most buoyant area.

"The Isle of Man is quite resilient because it is a well balanced economy and its financial services are spread across a number of disciplines," says John Spellman, the island's director of financial services. "It's a very challenging market out there and, like others, we have had job losses, but also, luckily, we have been able to generate opportunity."

The Department of Economic Development is developing a country-by-country strategy to win its share of wealth and corporate business in emerging markets, recognising that those such as China, India and the Middle East have differing needs. The

aim is to promote the range of services the island has to offer.

Its main pillars are banking, insurance, the fiduciary sector and investment fund management and administration.

Banking is the biggest employer with just under 3,000 staff. The island's 18 banks, like elsewhere, have struggled with the low interest rate environment and global deleveraging. Deposits have fallen from £57bn in 2008 to £47bn, but there are signs of stabilisation. Output rose by 4 per cent in 2010-11, according to government figures. Banking accounts for 11 per cent of GDP.

"It's not easy for anyone, but I'd say we are holding our own. We adjust to the environment," says Mark Waterhouse, chief executive of Zurich Bank International and chairman of the Isle of Man Bankers' Association.

There are hopes of attracting new banks from emerging markets to the island – and, even if that fails, says Mr Waterhouse, existing banks hope to offer services, for example, to Chinese companies exporting to Europe.

Insurance, employing nearly 2,000, has the biggest share of GDP of any sector of the economy at 14.7 per cent. Its output grew by 22.8 per cent last

year. The life assurance sector, which includes many of the biggest names, such as Royal Skandia, Friends Provident and Axa, is a big strength. Single life premiums from the UK have stagnated, but regular premiums for life and pension products in Asia and the Middle East are growing healthily.

"Future growth is going to come from the developing world," says David Kneeshaw, chief executive of Royal London 360° and chairman of the Manx Insurance Association. "It is really important that the Isle of Man is seen by regulators round the world, politicians and advisers, as a safe place to put clients' money."

The island also has a fairly stable sector of captive insurers, which insure risks for parent companies ranging from financial groups to utilities, manufacturers and airlines. Despite a "soft" global insurance market which does not favour captives, there has been an increase in inquiries about setting up new ones.

The fiduciary sector, which has about 1,900 staff and accounts for nearly 5 per cent of GDP, saw output grow by 15.6 per cent last year after a flat period following the economic crisis. It has 200 licensed trust and corporate service providers handling

business from family trusts to vehicles for owning yachts and aircraft.

"Those that have a more diversified presence are faring better than those that have their eggs in one basket," says Mark Denton, managing director of SMP Partners and chairman of the Association of Corporate Service Providers. "Some of the smaller firms may combine with others in the island or be swallowed up."

The fund management and administration industry, which employs up to 1,000, expanded rapidly before the crisis and has been hard hit since then. Funds under management have fallen from \$58bn in 2008 to \$22bn. But Ita McArdle, a consultant who chairs the Isle of Man Fund Management Association, has seen a shift in sentiment in the past couple of months.

"We are seeing a lot of new inquiries and a significant number of people converting it into business," Ms McArdle says. The island is particularly targeting early-stage funds in innovative niches.

Amid rapidly evolving financial markets, the Isle of Man must also cope with an ever-growing burden of global regulation, on which it is working closely with Jersey and Guernsey. The latest difficulties include the



Ita McArdle: targeting niche funds

US's Foreign Account Tax Compliance Act, a far-reaching law designed to smoke out tax-evading Americans holding money abroad, under which bank and investment details held by US citizens in other jurisdictions will be handed automatically to the US authorities. A deal similar to that reached between the UK and the US is likely.

The island is also considering carefully the impact of Sir John Vickers' UK banking reforms, which will ringfence banks' retail businesses from their investment banking

activities. One issue will be what flexibility, if any, banks on the island have over which of their activities are ringfenced.

The Isle of Man is also considering its approach to the EU's Solvency II insurance capital regime. It may seek equivalent status for its life assurance sector, but not for captives.

Companies must adapt to a rapidly changing commercial situation. Anthony Long, chief executive of Capital International, a family-owned provider of investment services, says the lengthy global downturn is "really starting to bite. We, and indeed the Isle of Man, have fared very well so far, but we have seen a flattening of our growth this year".

Its turnover had been growing by 15-20 per cent a year, but technological change is making UK rivals more competitive. That means the firm must deepen automation to cut its own costs, but there could also be opportunities as larger firms outsource operations such as custody and treasury.

"Financial services are still taking steps forward," says Mike Hennessy, chief executive of the Chamber of Commerce. "But it is a challenging environment, no doubt about that."

Food and drink enjoy growing reputation

Manufacturing

Andrew Bounds reports on industrial prowess across wide range of products

From apple juice to watches, space equipment to aircraft landing gear, the Isle of Man's manufacturing sector spans as wide a range as a country 10 times its size.

Making up 5 per cent of the economy and employing 3,000 people, the industry is enjoying the manufacturing resurgence worldwide. The island has an aerospace cluster, high-tech engineering businesses and a range of food and drink providers that are moving into exports.

The latest fillip came when its famous queen scallops were added to an EU list of more than 1,000 products whose names are protected by law.

Last year the Isle of Man "Queenie" won the UK Sustainable Seafood award after years in which Manx fishermen worked with the government to protect the marine environment. Now Brussels has added more protection for the Queenie by declaring it a "Protected Denomination of Origin", joining Champagne and Parmesan.

The island has a growing reputation for food and

drink: the Isle of Man Creamery's cheese is widely available in UK supermarkets.

One of the latest is the Apple Orphanage company, which produces apple juice. Its founders William Faulds, 28, and Charlotte Traynor, 28, met at Leeds University.

Mr Faulds had returned to the family farm – which he claims has the "wettest field on the Isle of Man" – and started making juice from the small orchard his parents kept.

He and Ms Traynor then hit upon an innovative idea – to source more apples from hobby growers who had more than they needed. In return for the apples, they would receive bottles of juice.

Ms Traynor recalls: "The first time we did it, we had people queuing round the block to drop off their apples. We must have had 10 tonnes of fruit."

For each 3kg, growers receive a 250ml bottle of juice. Many are single variety, such as the Andrew Johnson, only found on the island.

They made about 4,000 litres this year in a barn converted for the purpose and have planted their own orchard to scale up the business. It makes a profit, but not enough to support the pair, so they still live on the farm.

There are about 17 aerospace companies on the



Core activity: William Faulds and Charlotte Traynor make 4,000 litres of apple juice a year

island, including Ronaldsway Aircraft Company and GE Aviation, which makes landing gear but has been put up for sale by its US owner.

Eddie Teare, treasury minister, notes: "The evidence of water on Mars was found by a piece of kit made on the island."

Adrian Moore, head of

80%

Part of Target Tools' turnover accounted for by the aerospace industry

manufacturing at the Department of Economic Development, says the businesses are linked with the UK through the North West Aerospace Alliance. Some have 20-year contracts with Rolls-Royce for its new Trent engines.

The next challenge is to ensure there are enough

skilled engineers and the department is working with local employers to set up a training college. "There is a skills gap," says Mr Teare. "We are trying to upskill the younger section of our community. There are jobs. It is matching those unemployed with the opportunities."

Target Tools, a supplier of machine tools and parts, is a vital link in the supply chain, says Mr Moore.

Simon Radcliffe, director, co-founded it in 1994 to supply general engineering tools. But it has recently focused on aerospace, which accounts for 75 to 80 per cent of turnover.

"We have developed a lot of business in the UK. We have even sent tools to China for our customers," he says. Government grants for capital assistance and a zero corporate tax rate compensate for high transport and power costs," he says.

"There is great support for the industry on the island. If we have a problem we ring the ministry and

can get straight through to somebody who can help."

Bodystat, a maker of medical devices, has also grown with the help of government grants. Sakkie Meeuwssen, founder and chief executive, moved the business there from South Africa in 1990 in order to gain access to the European market. The machines can monitor the status of patients and are also used by athletes to measure their fat levels.

They are used by researchers looking for new drugs. Some hospitals and GPs are adopting smaller units for diagnostic tests. "I could analyse two patients with the same condition and tell you if one is going to die and the other not," Mr Meeuwssen says. Having just built a new headquarters outside Douglas, he says the company is on the verge of rapid growth.

"I would not like to be running a small business in the UK. With all the red tape and health and safety it must be a nightmare."

DLP Global maker of products for disabled and elderly

An industrial estate on the edge of Douglas, surrounded by outlets such as Pets at Home and double glazing salesmen, is the last place you might expect to find a global manufacturer.

Yet Tim Baker, finance director of DLP, a maker of kitchens and bathrooms adapted for the disabled and elderly, says it is the perfect location.

"It is a lightweight, relatively high-value product," he says, so the cost of shipping materials in and out is offset by the zero corporate tax rate. "It is a multipurpose manufacturing facility. It is small batches, flexible, with short lead times. We can take an order in the morning, schedule a product in the factory, have it out on the last boat of the day and it'll be in our Skelmersdale hub in the early hours of the morning."

The Isle of Man has worked for DLP, which trades under the AKW medicare brand. "We have been in the market for 25 years and are the market leader in the UK," Mr Baker says.

The company has a £40m turnover and 260 employees, with 70 on the island and most of the rest in the UK. All design, research and financial activity takes place on the island as well as some assembly. Units are sent to the main manufacturing and distribution facility in Droitwich.

It sells mainly through occupational therapists, who recommend products, and to charities and councils running care homes. "They choose by brand or brand equivalent so you have to get yourself on the list. If

you can modify people's homes, as their mobility reduces, they can stay there longer. Most people want to stay in their own home and it is an awful lot more cost effective for the state," he says.

The UK accounts for 90 per cent of sales, but DLP also sells in Belgium, France and other European countries. It has a distribution agreement in the US and is hopeful of fast growth there.

Mr Baker admits the UK public sector budget cuts have hit sales but he believes an ageing population offers massive potential.

"Increasing longevity gives us a great opportunity. It has been a niche market. What we see happening is people, as they are having to provide for themselves, will move into a future-proofing mentality."

That attracted ECI Partners, a private equity house, to back a management buyout in 2008.

There are 5,000 products because of the differing sizes of showers and kitchens. They include shower screens with small windows for carers to gain access. They have to be tough enough to



Functional but attractive

support a wheelchair.

AKW was established in 1990 in Worcester but started shower tray manufacturing on the Isle of Man in the 1990s. It then moved into kitchens. Now the challenge is to create products that are not just functional but also attractive. They include a built-in hob that can be lowered for a wheelchair user.

A small team of designers works above where the fibreglass shower trays dry, testing taps, smashing worktops and creating new products.

The latest is a shower for the partially sighted. Big buttons feature Braille and it is incapable of getting to a scalding temperature. The head swivels while still in the holster, reducing the chance of it being dropped.

While much production is mechanised, the final assembly is labour intensive, with workers standing at counters to add joints and seals on to shower screens.

The government has given grants towards new machinery, part of its package to help manufacturers.

"We provide the kind of jobs needed on the island," says Mr Baker. "Not everyone wants to work in an office." The company has taken on several young unemployed and unqualified workers to give them a chance under another government supported scheme. "There is a strong work ethic in here," Mr Baker says.

"We have great growth opportunities. The challenge is to make the right choices."

Andrew Bounds

When the Department of Economic Development were looking for a new direction, we showed them 'Where you Can'.

We are delighted to have played a major role in researching, developing and implementing the Isle of Man's brand positioning.

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Asia internet gaming on a roll

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cent on the first £20m of gross gaming yield annually. There are 47 licence holders but Mr Crane says the policy objective is "quality, not quantity".

Industry executives agree that the US move against Manx-based PokerStars, which runs online poker rooms, for money laundering, illegal gambling and bank fraud, has reinforced its reputation.

PokerStars struck a civil settlement with the US Department of Justice in July, paying back \$571m to the government and reimbursing the non-US players of Full Tilt, a rival, for \$184m but admitted no wrongdoing.

PokerStars acquired the assets of Full Tilt, which was also charged, as part of the deal. While PokerStars' players had been protected by the Manx regulator – which insists clients' money is kept in ringfenced accounts – those at Alderney-based Full Tilt were out of pocket until PokerStars took it over.

Anxious not to miss out on gambling revenue from its own citizens, the UK is proposing a move to a "point of consumption" model in which money would be levied depending on where customers are, not where the businesses they bet with are. "Globally there is a move towards tax and regulate. Governments are looking for new ways to generate revenue."

Manx regulator insists clients' money is kept ringfenced

He believes the EU, where member states operate as individual markets, will eventually create a single market in betting.

Garth Kimber, the government's former egaming ambassador, was headhunted by Xela Holdings, another Asian company, last year to establish a base on the island. He says the company wanted access to Europe and the possibility of listing there one day.

However, he says most of

Doing Business in the Isle of Man

Changed tax deal puts squeeze on growth

Economy Rare for the developed world, the island has escaped recession but it is nonetheless feeling the fiscal pressure, reports *Andrew Bounds*

With growth running at 3.4 per cent in 2010-11 and estimated at the same rate this year, the Isle of Man is one of few areas in the developed world to have escaped recession.

While its financial services industry has shrunk slightly – its share of gross domestic product has remained stable at about 35 per cent since the financial crisis – other sectors such as egaming and manufacturing have achieved strong growth.

Nevertheless, it is feeling the fiscal squeeze as much as its neighbours in Ireland and the UK after the loss of about £200m a year in value added tax revenue from changes made to its “common purse” sharing agreement with the UK that are less favourable to the island.

GDP stood at £3.5bn in 2010 and the island has no debt. Inflation has begun to fall sharply after increases in VAT, food and energy prices are filtered out.

Eddie Teare, treasury minister and a retired senior banker, says: “We are still growing, although it is an economy of two halves. The economy that faces out to the wider world is growing well but the one that is dependent upon the local spend is coming under pressure. There is pressure on the construction industry, hotels and leisure. But we are still creating jobs.”

A national insurance holiday for companies taking on staff has created 250 new jobs.

“The overall level of unemployment is still low at 2.2 to 2.3 per cent but I am not complacent.”

Mr Teare has outlined a four-year plan to balance the budget, using £91m of its £1.5bn reserves to cushion the blow.

“We are looking more at spending cuts in a measured way,” he says.

“This year, we are using £55m from reserves, 1.5 per cent of GDP. I felt that was as much as we could do in one step. It is a fine line between cutting and impacting on business confidence.”

The budget should be balanced by 2015-16. The cuts will amount to £214m with £26m tax increases and £103m in spending cuts.

However, he says retaining joint value added tax arrangements with



GDP stood at £3.5bn in 2010 and the island has no debt

the UK was vital for competitiveness.

“It gives us advantages for companies that want to establish companies in the UK,” he says. “The Isle of Man can handle all VAT affairs. Traders can talk to the one VAT office.”

VAT changes have had other effects. Its successful shipping register, which generates income for corporate services providers, has been hit by a change made by the UK five

years ago. Owners of yachts who want to register them on the island for VAT purposes, allowing the VAT bill to be paid over the 20 year life of the boat’s mortgage, now have to visit the island to be eligible for the benefit.

Chris Allix, director of Dominion Marine, who has been registering and managing yachts since 1984, says the changes had allowed Malta, which did not have the same

requirements, to win some business.

Most Isle of Man companies have now had to open outposts on the Mediterranean island, he says, incorporating the yacht company there but using the island for back office work.

“You will still use the Isle of Man but not for everything,” he says.

The number of superyachts registered has hovered at about 100 since 2010.

Foreign visitors flock to the Manx Grand Prix motorcycle races

Tony Goldsmith

Dick Welsh, director of the island’s ship registry, says the registry has continued to gain ground with larger boats, thanks to its quality service and low fees, overtaking Norway and the US to become the world’s 15th largest.

Fees are charged at a flat rate, whatever the size of the boat. It had 436 merchant ships at August 31 and a total tonnage of 14.3m.

The maritime industry employs about 580 people with average salaries of £35,000 and £20m in local spending.

The aircraft register won its 500th customer this year.

It has had much success by enrolling leased aircraft while parked or between customers, says Hartley Elder, director of civil aviation.

The island is hoping to enter the renewable energy market.

Ken Milne, of the Department for Economic Development, says it is negotiating with wind energy producers to extend the Irish Sea farm into the island’s territorial waters. It owns the seabed. But the island’s 90MW demand is too small for such wind farms so it would need a deal to supply surplus energy to the UK.

Meanwhile, Sefton Group, the country’s biggest leisure group, says it is performing strongly. “We are a microcosm of the Manx economy,” says Brett Martin, chief executive.

While business travel is down, its four-star Sefton Hotel, Palace Hotel and Casino and Sefton Express budget hotel by the airport have benefited from robust local spending.

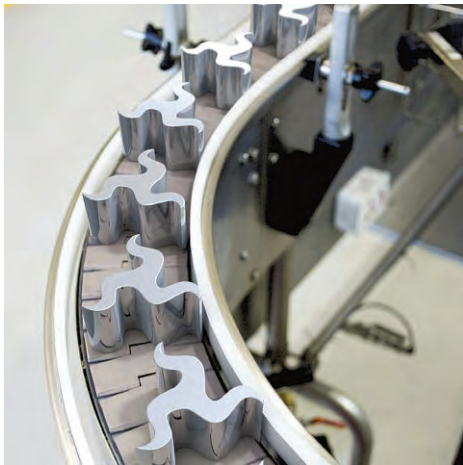
Mr Martin says Manx residents still had cash to spend, and with fewer splashing out on foreign holidays, more were taking cheap breaks in Douglas for the theatre or other events.

The group made a modest operating profit but fell to £6.3m loss in 2011 because of interest rate swaps and losses on property sales.

Mr Martin says events such as the Manx Grand Prix motorcycle races and the End 2 End mountain bike race across the island were attracting more and more foreign visitors.

Mr Teare says the government will do more to promote these.

“We have got to recognise that people come here for the scenery and activities.”



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Doing Business in the Isle of Man

Under pressure over the morality of tax planning



Brian Groom

Many countries and other offshore centres would envy the Isle of Man. Amid global financial turbulence, its economy grew by 3.4 per cent in 2010-11 – a 28th year of continuous expansion – and it is estimated to be performing similarly well in 2012.

The island's inhabitants are acutely aware, however, that they cannot afford to be complacent. It faces four notable challenges.

First, it must continue to show the adeptness that has allowed it to develop niche opportunities to diversify its economy in fields such as e-gaming, space and advanced manufacturing, along with aircraft and shipping registries.

Second, it has hard choices to make to balance its budget by 2015-16 after the shock in 2009, when the UK Treasury rewrote the “common purse” agreement that determines how revenues from value added tax are shared, cutting government income by about £200m a year.

Third, it needs to market itself effectively, particularly in financial services, to claim its share of the market for managing the growing wealth in Asia, the Middle East and other emerging economies.

And fourth, it must continue to respond to international pressure against low-tax financial centres, which is strengthening because of the higher taxes and drastic spending cuts that people in larger economies are suffering.

That pressure is entering a new phase: people are questioning not just the legality, but the morality of tax planning. Allan Bell, chief minister, recently told Tynwald, the island's parliament: “This change in attitude is being played out in the media, on the streets of capital cities and in political actions that we ignore at our peril.”

Manx people have a history of resilience and pragmatism. One of its strengths is that, for an island of only 81,000 people, it has a remarkably varied economy.

That did not come about by



accident: it has painstakingly set out to exploit new niches so as to avoid over-reliance on financial services. E-gaming alone now accounts for 9.7 per cent of gross domestic product.

Space is the most eye-catching niche. An array of aerospace, space tourism and satellite communications businesses is located on the island. It could even win the race to fly a tourist around the Moon after Excalibur Almaz, a locally based

company, says it will be ready to take passengers on private lunar expeditions by 2015. The sector is forecast to generate £1.7bn turnover over the next three years.

What has helped the island to develop these niches is its ability to move quickly in creating the right legislation and regulation. Other jurisdictions are latching on to this technique, however: the time available to exploit a niche before

others leap in is getting shorter.

The financial sector, which still accounts for 35 per cent of GDP, is itself diverse, with four strong pillars: insurance, banking, fiduciary (trust and corporate service providers) and investment funds. Strong growth in life assurance is more than making up for a flat picture in banking and a decline of funds under management.

The island's attractions include not

Space age: sector is forecast to generate £1.7bn turnover over the next three years

Charlie Bibby

just low taxes, but also proximity to the City of London – through which it gains much business and to which it contributes capital flows – along with pragmatic regulation and a wide range of expertise.

It is stepping up marketing in emerging economies with a country-by-country strategy that recognises that what works for India may not do so for China or Abu Dhabi.

Some think the Isle of Man was slow off the mark: its success will depend on how well it can harness the range of products and services it offers.

In meeting its fiscal challenge, the government has already made some tough decisions. It has squeezed mortgage interest relief and announced that universal child benefit will be means-tested from April 2014.

The government is cushioning the fiscal squeeze by drawing on reserves over the next three years, but expenditure has to come down

Excalibur Almaz, a locally based company, said it would be ready to take passengers on private lunar expeditions by 2015

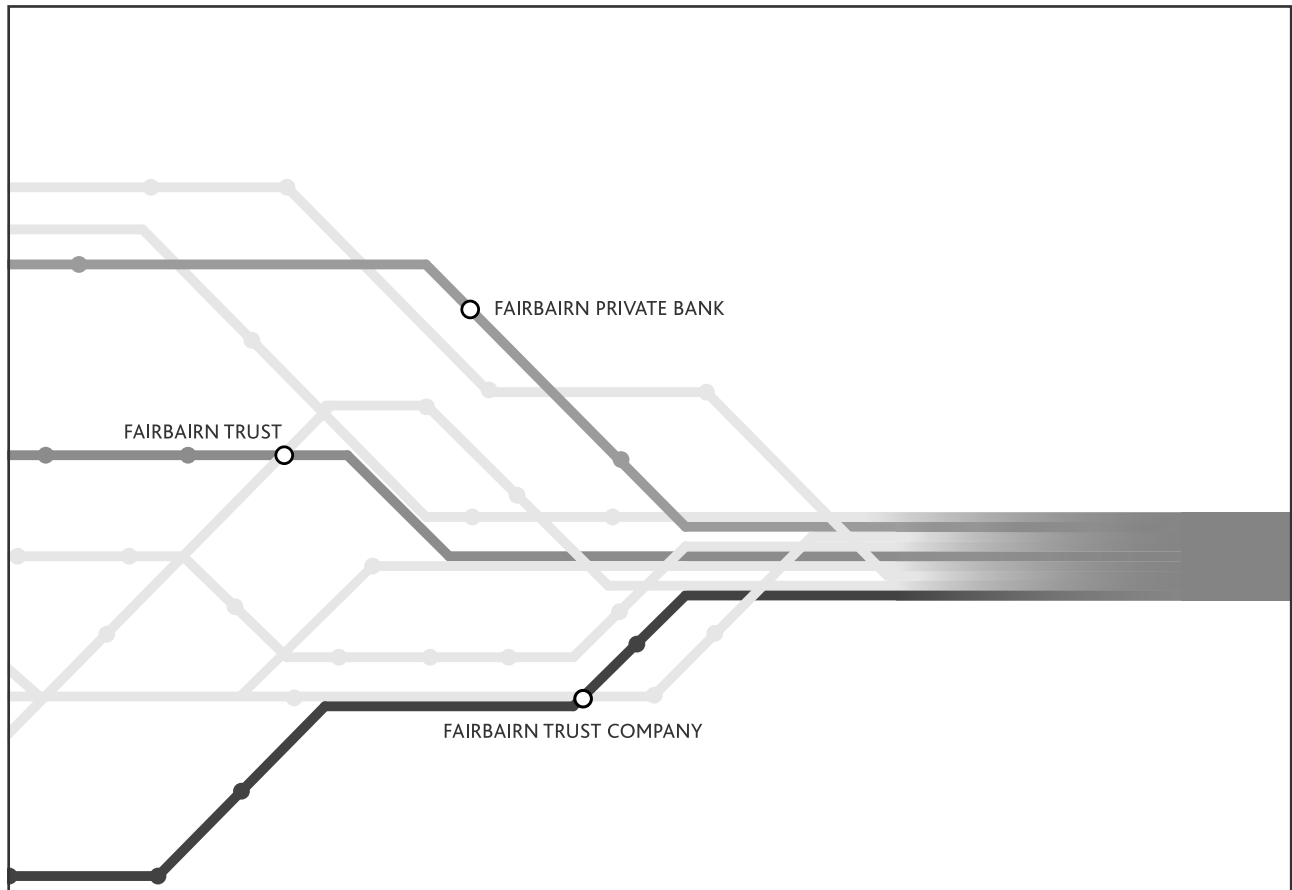
further, which means rethinking elements of its generous welfare state.

It is aided by the fact that most of its politicians are independents, so it is a judgment about fairness rather than an ideological battle.

Meeting global pressure against tax havens is in many ways the hardest task, even for a co-operative jurisdiction that has for more than a decade tried hard to meet the requirements of the EU, OECD and the International Monetary Fund.


It is not easily ducked. Abiding by the rules is one thing, but one person's aggressive tax avoidance is another person's legitimate tax planning.

Asked how the island would react if one of its companies was accused of the former, Mr Bell says: “We would be very concerned if we were seen as being used for that purpose and I am sure we would take appropriate action to ensure the loopholes were closed.”




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Sector grows in sophistication, experience and global outlook

Professional services
Brian Groom finds diversification into pensions advice and management of yachts and aircraft

As the Isle of Man's economy diversifies, so too its professional services sector is expanding beyond law and accountancy to advice on areas such as pensions, yachts and aircraft management.

It feeds off the growth of financial services and other sectors, but also acts as a conduit to bring new business to the island.

“The accountancy profession works with the legal profession and the banking profession,” says Eddie Teare, treasury minister.

“If an international organisation is thinking of doing business through the Isle of Man, we have the expertise here to act as a one-stop shop.”

Like other sectors, it been affected by the global economic slowdown.

But it is growing in experience, sophistication and international outlook.

All the big four accountancy firms have sizeable operations, along with others such as PKF, Moore Stephens, Baker Tilly and

Grant Thornton.

David McGarry, KPMG's Isle of Man managing director, has seen his staff grow from five to 110 since 1982.

He acknowledges that things have got tougher since the financial crisis.

“We have not had a dip [in turnover] but we are not growing at the rate we were four or five years ago.”

Capital markets business has slowed and clients are driving a hard bargain on audit fees.

But many accountancy firms have expanded in areas such as tax planning, value added tax and advisory services.

Mr McGarry says: “We try to support our clients as they grow, but also to bring new business to the island. I spend a lot of my time out promoting the Isle of Man as a location for funds.”

The biggest event in the legal world in recent years has been the arrival of Appleby, the world's largest offshore law firm in terms of staff, via a merger with Dickinson Cruickshank, an Isle of Man firm.

Brian Johnson, director of Appleby Aviation, a new subsidiary, was previously director of civil aviation for the island.

He says the island, with its UK value added tax registration allowing access to the EU, and bespoke company law for owning aircraft, had become a world

leader in aircraft registration.

“When the register first started, we thought there would be 12 in the first year. We have had 500 aircraft in the first five years.”

Each aircraft brings between £15,000 and £20,000 in annual revenue to corporate service providers,

‘Russian clients are very demanding but if you provide the service they will stay with you’

banks and advisers, he says.

Mr Johnson says Appleby had “done extremely well with Russian clients. They are very demanding but if you can provide the service they will stay with you”.

Cains, another island law firm that has been in business for more than 100 years, achieved revenue growth of 3.5 per cent last year – below the 10-12 per cent it was achieving before the crisis, but not bad in a difficult climate.

Profit was up by 8 per cent before exceptionals.

Virtually all the firm's business is international, much of it in eastern Europe and southeast Asia.

Cains has built a reputation as legal adviser to Russian and Indian companies coming to list in London.

The island has become a bigger host of non-UK Aim companies than any other jurisdiction.

That work has dried up since 2008, but Cains is still winning work on debt issues in markets such as New York and Singapore, in which the offering entity is an Isle of Man company.

Other work comes from wealthy families or companies in growth areas, plus some restructuring work on companies in trouble.

Andrew Corlett, Cains' managing director, says the attraction of listing via an Isle of Man company is “a system of law which is readily understood by advisers around the world, acceptability for the listing authorities and tax transparency in terms of no withholding tax on any coupon”.

Simcocks, another law firm, has seen turnover fall by 25 per cent since 2008 and staff shrink from 60 to 50 as work emanating from London has slowed.

But Phil Games, chief executive, says it is fighting back by expanding into the British Virgin Islands.

Two of Simcocks' staff have qualified as BVI lawyers and it will open an office there early next year.

The aim is to provide legal advice to BVI companies managed by local corporate service providers – a model that could be replicated in other jurisdictions with an English common law base.

Some count the regulated professions working for trust companies and corporate service providers as part of the professional services sector.

These are, in any case, developing into “solutions-type businesses”, says Mark Denton, managing director of SMP Partners and chairman of the Association of Corporate Service Providers.

“The CSPs that will do better are ones that have accountancy and tax capability, VAT capability and provide a fuller service.”



Cains law firm: virtually all of its business is international, much of it in eastern Europe