Isle of Man Government

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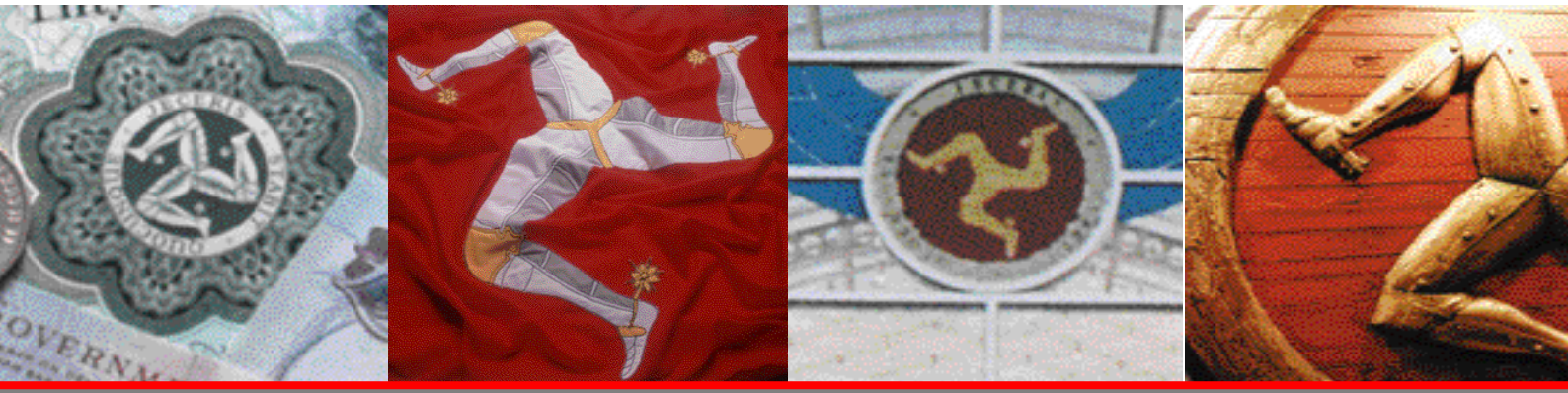

The Potential Introduction of an Enterprise Development Scheme to the Isle of Man

Review of Consultees' Comments

Department of Economic Development

October 2015

Summary of Responses to the Consultation on proposed Enterprise Development Scheme[1]

Public Consultation period: 22nd July to 3rd September 2015

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[1] During the Consultation process it was decided that the Enterprise Development Fund was to be referred to as Enterprise Development Scheme in line with other Government schemes.

1. Background

The Department undertook extensive research on as to how growth in the Island's economy can be stimulated, resulting in the document Vision 2020 published January 2014. One of its conclusions was that the Isle of Man is a diverse international business centre and, over the last 10 years, had increasingly attracted high-growth Small & Medium-sized Enterprises (SMEs) delivering services worldwide, often via electronic channels.

Since that time, further work has been underway to deliver on the 8 key strategies in Vision 2020. One of these strategies, named Enterprise Isle, was aimed at providing more effective and holistic support for high-growth SMEs to achieve their potential. In support of that strategy, we have sought to improve our offering to new and expanding businesses.

The recent "Consultation on the Proposed Enterprise Development Scheme" highlighted the following points as important to the Isle of Man's economic development:

- In order to sustain and improve the Isle of Man's future economic position the Island needs to create new jobs and new economic sectors. As the economy changes shape and the existing demographic mix continues to age, it is important that the Isle of Man generates new economic activity.
- The Government estimates that 500-1,000 jobs are needed to balance the demographics and to fund future services and replenish fiscal reserves. It is anticipated that a part of this growth may be achieved by direct support and / or investment, such as this Scheme, into the Isle of Man economy.
- The Isle of Man economy has maintained its resilience by creating a stronger and more diversified offering than many of its competitors. The creation of such an environment only comes about by offering meaningful advantages to entrepreneurs and businesses that are essential to attract new businesses and nurture entrepreneurial ambition.
- Businesses often encounter difficulties in raising early stage finance. The Department believes there is a case for investing public funds to help to attract such businesses, helping them to grow and so generate jobs on the Island. The Consultation was intended to seek feedback on the proposed EDS in such a manner that it provides targeted support whilst also meeting the specific needs of the businesses concerned.
- The Department feels that it is also appropriate to support growth in existing sectors and create new opportunities through Government led incentives.
- The Scheme proposals looked to evaluate the viability of a scheme on the Isle of Man that will deliver targeted finance to Island based firms and those wishing to relocate to here. The target size of the funds committed to this undertaking would be up to £50 million over a 5 year period.
- The proposed EDS would offer either grant, loan or equity based support, depending on the business type and the business growth they hope to achieve. It is not intended to provide subsidies for businesses with trading difficulties nor speculative enterprises.

2. Summary of responses

The Department of Economic Development received a total of 33 responses to the public consultation. There was feedback from a variety of sources broken down as follows:

17 Businesses, 8 Individuals, 5 Associations, 2 Banks and 1 Local Government Authority.

These were felt to provide a broad range of views and suitable to use as a basis to propose alterations to the proposed Scheme.

3. Executive summary

Overall, the feedback from the Consultation was supportive of the creation of a range of business support measures in addition to the current schemes. The principle supportive comments included:

- "The existence of the proposed fund will no doubt increase the attraction for the island to new start-ups." Increasing the number of start-ups should deliver good quality jobs that will provide tax revenues and encourage growth on the island.
- "The Isle of Man is competing against other similar jurisdictions and UK regions for inward investment." By having an EDS, the Island will be more competitive compared to similar jurisdictions, resulting in the Island becoming more attractive as a jurisdiction to set up business.
- "The EDS will allow the Government to pro-actively participate in growth of the economy." Other Governments have been able to assist in creating economic growth, with markets benefitting as a result of Government investment.
- "The addition of a further source of funding, via grants, loans or equity will undoubtedly help to attract these businesses to the Island and be critical to the goal of attracting start-ups to the Isle of Man."
- "In the current economic climate it is frequently difficult for start-up, expansion, and relocation to be viable without such targeted investment."
- "we consider that the creation of the Fund will be a fantastic addition to the armoury Government can give itself to achieve its strategic goals to continue to diversify the economy"

The principal concerns that were raised by respondents included:

- The risks associated with lending to companies who had been rejected by the private sector, noting they will have been rejected for appropriate reasons. The basis of consideration of lending support has been changed in the Guidelines on the basis of this feedback. It is important to note that under the proposals Government will only be a minor investor (typically up to 20%) so if the business concerned is unable to secure most of its funding from the private sector then it will not receive any public funding.
- Ensuring that the politicians and the general public were kept informed on the activity, performance and success of the Scheme. This Government understands that there is a

threat to reputation and undue political interference should misunderstanding of performance occur. It is committed to being transparent on the performance measures.

- That adequate portfolio diversification should be made in order that there is spread of risk to minimise the effect of an economic downturn and individual business or sector failure. This will be agreed in the mandate between the Government and Scheme Manager.
- That the Scheme will displace existing economic activity from one company to another and not actually benefit the local economy. Further, the scheme needs to consider all sectors of the Islands economy in order to ensure there is growth through all sectors. The Scheme guidelines address this concern and allow discretion to consider individual business circumstances.
- Concerns over the expertise of the Investment Manager (now Scheme Manager) and the need for local economy knowledge were considered vital to ensure the Scheme Manager performs in the interests of the island. The Government accepts that the structure needed is one that allows the Scheme Manager(s) to make independent decisions while allowing Government to set the mandate to establish what is in the best interests of the island. Further, it will propose that an independent form of accountability is maintained including a right of appeal in the process.

As a result of the Consultation, a number of amendments to the original Scheme design have been incorporated into the current proposals in order to ensure accountability, the ability to challenge decisions, the right of appeal and transparency.

To enable the powers required by the EDS, amendments to the Financial Provisions and Currency Act 2011 have been prepared separately for consideration by Treasury.

4. Consultation responses

Q1. Do you believe there is a need in the local market for an Enterprise Development Fund with a mandate to invest in local businesses and attract new business to establish here?

The large majority of respondents (24 of 33) were in agreement that there is a real need for additional investment and support that would be provided by the EDS.

The remaining were split negatively (5) and neutrally (1). 3 respondents did not comment on the need for the scheme.

Comments included:

- "There is a need to attract inward investment to create jobs and additional tax revenues and in principle is supportive of the introduction of an Enterprise Development Fund."
- "The EDF is welcomed as a mandatory and state-of-the-art building block in a comprehensive toolset to support and grow businesses, as established in other jurisdictions already. Its envisaged budget of 50 million GBP in relation to the islands population is a bold statement."
- "No, there is no need for this proposed fund."
- "Absolutely key to obtaining a competitive advantage and shaping the IOM economy."
- "The additional support provided by an Enterprise Development Fund (EDF) to local businesses would have a positive impact on the Island's economy."
- "To stimulate investment that will create jobs and income on the Isle of Man is supported wholeheartedly."

Q2. What benefits do you envisage for the Isle of Man?

The majority of respondents (19) highlighted job creation through new businesses or expansion of existing business as the main benefit to result from the implementation of an EDS, which ultimately leads to knock on and multiplier effects through the Manx economy.

Other notable replies included promoting the Isle of Man as an attractive location for new businesses and a more dynamic business sector.

Comments included:

- "Employment of the right type".
- "a more focused tech economy and an ability to attract start-ups and small companies (the wealth creators rather than the wealthy)"
- "Creates higher quality jobs that are net contributors to the fiscal balance."
- "The EDF should be strategically dedicated to foster transition from growth driven by eGaming to a broader and less vulnerable ICT economy."

- "EDF should make the Isle of Man more attractive as a jurisdiction to set up an Isle of Man business. The EDF may result in additional employment in the Island, both from within existing Island based workforce but also by bringing additional skilled workers into the island."
- "The principle objective of a new EDF is that the investment should lead to increased tax revenue and new jobs."
- "Because we do not have access to the majority of EU or UK government funding options for enterprise development, by stepping in with the EDF our government will help to level the field for our economy."

Q3. Do you think the Government should offer grant, loan and equity support or not? Please give reasons for your answer.

Of the 33 responses, 16 replied positively to grants and outlined that the existing system FAS (Financial Assistance Scheme) works well. The existing grants system will continue to run alongside EDS. There was strong support for loans (19), including where the existing providers have not been able to support applicants, in particular the idea of co-lending at pegged interest levels. Equity funding was well supported (18) arguing that there is an ever increasing demand for support of this kind from governments.

10 respondents did not provide a response.

Comments included:

- "Government should have the facility to offer grant, loan and equity support where value and opportunity can be identified according to goals of the Government."
- "The case for grants is weak and is too generalised. I do not believe this represents value for taxpayers' money."
- "Loans, yes but not where it competes with the private sector. All loan opportunities should be put to a panel of banks before government lends."
- "Equity this is the key constraint for a company. As a result it is a key tool for attracting early stage companies. It also represents the greatest upside for government."
- "This is a key strategy that is currently somewhat lacking from the traditional banking sector at present, it may subsequently, if successful encourage inward investment from banks and other entities."
- "The focus on the EDF should be equity based, as this allows selection of the best companies to invest in after proper due diligence, to achieve the highest potential ROI."
- "Grants are all very well but larger equity funding may be preferred due to long software product development cycles - founders need money that will enable them to live for a period on a shared risk basis."
- "The EDF should not be involved in lending in any way."
- "In order to provide flexible solutions to various business needs, a wide offering of tools like public grants, loans and equity is appropriate."

Q4. What features in the proposals do you support and which aspects do you feel inappropriate in the various schemes described above?

The key feature supported was creation of jobs (13). There was further support for the need of in depth due diligence and analysis of business plans to ensure that the fund is spread across the best ventures to support the Island's economy.

A remark was made in which £3,000 to £5,000 grants for the SBSUS is insufficient suggesting a higher level of £10k would have more impact. This was echoed by further respondents (3). Similar questions were raised over the finance limits used in the proposal, which have since been amended.

Further questions were raised over the lending, whereby the private sector had already rejected the business plan. The basis of eligibility has now been changed and the Scheme Manager / DED would review the reasons for rejection as part of the application.

There was a suggestion that as the loan applicants had been rejected previously by a bank that there is a higher risk associated with the loan. Instead the loan could be issued over a longer term, or alternatively, have a higher interest rate pegged to associate the increased risk. The basis of consideration of lending support has been changed in the Guidelines.

A suggestion was raised for the need of an Advisory Board as some individual investment managers or companies may lack essential local market knowledge and business networks. The Scheme proposals now include the provision for an Advisory Panel as a referral mechanism to ensure that specific industry expertise can be delivered.

Comments included:

- "I feel that the proposals are pretty clear and appropriate in their entirety."
- "We feel the proposals are most suited to new businesses to the island, existing businesses which are export focussed and small businesses in the start up phase which are also export focussed."
- "All three phases of business will benefit from support."
- "Generally good to make different types of provisions available to different types of enterprises and offer proportionate funds to whatever criteria is used to evaluate and select them."
- "It is vital that where businesses are trying to establish in the island and have been approved by the scheme, assistance is given to enable them to employ appropriately skilled staff from off-island, if necessary."
- "We believe that the investment criteria should focus on supporting businesses that will generate tax revenue and create new jobs."
- "We feel that off-island fund managers should not be involved in investment decisions for small businesses in the start-up phase."
- "Be aware of fair competition versus displacement. Support the growth of our existing businesses to become more profitable and able to reinvest."
- "In order to lend the maximum figure of £100,000 it is likely that the turnover cap of £150,000 should be set significantly higher."

- "It feels inappropriate to support domestically focused businesses unless they are considered strategically important and unique in providing service in their field."
- "We are concerned that the extent of exclusions should be very carefully considered. We say this as one of the main criticisms historically of the IOM for incoming residents and businesses, was the lack of good restaurants and retail."
- "Small businesses in the start-up phase focussed on Island. This is essential. If nothing else, it will breed entrepreneurs."
- "While generally split into three tiers in this document I feel that the amounts proposed for the first two tiers are unrealistic in the real world and the ancillary support that is needed is not made available to incubate seed businesses on the IoM."

Q5.Based on what criteria do you think the Governments advisers should base their investment decisions?

i**) as a standalone business**

ii) plus the wider benefits to the economy

iii) other criteria (e.g. job creation)

The majority of responses (17) indicated that there was a need to weight investment decisions across the three areas, with arguments included that the Government should be encouraging all growth areas that will provide benefits and multiplier effects through the economy.

3 respondents supported standalone business. 1 response gave point's ii and iii as the criteria for investment decisions. 1 response argued that Government should make the decisions.

11 did not provide a response.

Comments included:

- "Public funds invested should have the best possible return for the economy. The funds should be invested as a priority in those businesses which will be providing economic benefit to the Isle of Man."
- "We need to appoint an experienced investment manager with experience and a successful track record in this market. They should be incentivised to earn fees from success not simply for managing invested funds."
- "The EDF should consider all of the above, plus others such as interaction with other on island businesses and the ability to open new markets or cooperation opportunities in different territories."
- "I strongly believe that the Government should manage its own fund. Professional fund managers are not investors 'for the people'."
- "Utilising an investment manager based in the UK or elsewhere would be wholly inappropriate for several reasons – lack of local knowledge and expertise and effectively,

EDF funds would leave the Island in the form of management fees paid to the investment manager."

- "They should not make any decisions! They should give their advice to Government, which should thereby remain accountable to the people, and Government should make the decisions based on this advice."
- "Robust analysis of company business plans during the due diligence period will be critical to select the best investment opportunities."
- "Given that the EDF is funded from tax payer reserves, the fund's investment criteria and decisions should include the wider benefits to the economy."
- "The EDF should have the potential to support a diverse range of businesses."
- "As this will essentially be a State Fund it should ensure that its advisers have regard for all of these criteria."
- "All three and the fit with the Island generally. The criteria should be publicly available and fit with the vision of Enterprise Isle."
- "I feel that all the criteria should be applied on a sliding weight system depending on the individual case circumstances."

Q6. Should the EDS be able to only support specific sectors (e.g. export based) or all Isle of Man based businesses depending on the quality of the Business Plan? If so, which and why? Please give reasons for your answer.

Out of the respondents, an important recurring theme running through the responses (11) were that **all** Isle of Man based businesses, depending on the quality of the business plan, should be supported.

One response was neutral in that it trusted the government in determining matters.

One response highlighted that the Island is too small to support specific sectors and a general approach was therefore required.

Two responses supported export based companies exclusively. Another supported new sectors and export driven businesses, but not exclusively.

Comments included:

- "The EDF should be able to support a wide cross section of businesses. Export income is good, tourism helps us showcase the island and the local pound spent also supports demand, job creation and improve the infrastructure of the island for the benefit of everyone."
- "Businesses within specific sectors should be considered more favourably where there has been a strategic decision by DED to invest in developing those sectors in the Isle of Man."
- "The quality of the business plan should be paramount."
- "I feel that all Isle of Man based businesses should be considered, depending on quality of the business plan and potential."

- "Needs to be flexible as to sectors, stages of business and whether they are exporting or serving local market."
- "The Fund should only support businesses generating profits off-Island."
- "We consider that all business opportunities should be considered if they are going to contribute positively to IOM"
- "The EDF should support all sectors of the economy providing that the business plans are of sufficient quality and that the investment does not create an unfair advantage over existing island companies."
- "The government's advisers should base their investment decisions on standalone viability, benefits to the local economy and job creation."
- "Export only."

Q7. What risks do you see in providing such a scheme? Please expand your response where appropriate.

There were a diverse range of answers to this question, with multiple replies citing there are always inherent risks associated with investments.

A couple of responses to this question outlined the importance of securing the right investment manager, whilst also raising concerns over ensuring the independence of the investment decisions; to ensure the decision making process is free of political interference to ensure the effectiveness of the business decisions.

There were also concerns raised that diversification of the apportioned money was also stressed in order to minimise portfolio risk. Comments included:

- "An inherent risk of any such public funding schemes remains in failing to guarantee the independence of the investment decisions."
- "It is imperative that the right third party investment manager is appointed."
- "Making a large investment could restrict the funds available to provide sufficient diversity of investment within the fund to minimise the risk of the portfolio effect."
- "Compliance and exit risks."
- "Scheme could become self-limiting (too narrow sector selection)."
- "Lack of public understanding of the goals of the fund."
- "We would suggest that the portfolio needs to be relatively broad in number and also contain a diversity of sectors. This is to avoid single name risk and sectorial downturn."
- "The obvious risk is none of the borrowers provide the anticipated return."
- "Some investments will inevitably fail and there needs to be a very clear mandate that accepts this will be the case and from the outset."

Q8. The scheme offers small start-up and commercial loans, do you feel these would complement rather than compete with the existing lending market locally? If so, how could the scheme be used to complement traditional providers of finance (i.e. banks)?

Of the 33 responses received, 17 answered the question. 11 suggested the scheme would complement rather than compete with the existing lending market, with one reply pointing out that the scheme may in turn act as a catalyst for the banking sector.

2 responses were neutral, suggesting the competition factor would be decided on the structure of the loan.

3 responses suggested that the scheme would compete with the existing lending market.

One response argued that the Government should not be in the lending market with public funds.

Comments included:

- "A lender may well be reassured that they are lending more securely if for instance a small business start-up has secured scheme funding and therefore has undergone further scrutiny and rigour in proving a safer case for receiving a grant/loan."
- "This depends on the structure of the loans, their interest rates and the liabilities. Working together hand-in-hand with banks, taking risks and liabilities for the ventures would immediately solve that problem and save the islands direct liquidity in the EDF."
- "Should complement - joint financing of a start-up project."
- "The scheme should complement existing lenders."
- "The small start-up and commercial loans would certainly complement the existing lending market."
- "the EDF should not be involved in lending in any way."
- "Government should work with the private sector to raise debt on a case by case basis. This ensures that a) the fund is skewed towards equity which creates most value in attracting business here and b) doesn't compete with the private sector and damage the local economy."
- "The scheme would compete with the traditional providers of finance."
- "We do not see that the Fund would do anything other than assist in complementing what lending is still available and should not consider itself to be in competition with existing lenders."

5. General comments

The following notable comments were also received:

- "We must recognise the importance of a solid foundation. The initiatives in the Enterprise Isle will only truly succeed if those are built atop reliable technical bedrock of fast, free, universal broadband and digital-friendly business requirements."
- "One matter which isn't raised above, but will be vital to the success of the EDF, will be an organised, high quality incubator offering. This should be made available, as part of the EDF, to aid companies moving to the island."
- "My suggestion would be that at least part of the proposed funds would be better spent on improvement of the business infrastructure."
- "No mention is made of regional investment to encourage economic activity in areas outside Douglas when those areas are recognised as being areas with higher unemployment and higher levels of deprivation."
- "The EDF could be used to help new businesses offer relocation packages particularly where skills and talent are not available on island."

One respondent discussed the concept of Government establishing a state owned bank. Whilst noting the suggestion, this is not part of the EDF scheme proposals and was, in fact, addressed separately as part of the Alternative Banking Regime consultation.

The Department acknowledges all the additional comments made in support of improving the wider business infrastructure, and many of these initiatives are being addressed as part of the wider Enterprise Isle programme, e.g. areas suggested included broadband coverage/quality, flights, costs of power and other utilities.

6. Conclusion

The Consultation has provided many well rounded arguments, giving the Department the necessary input to improve the Scheme's design. Where challenge has been accepted, we have proposed amendments including building in accountability, the ability to challenge decisions, the right of appeal and reporting to ensure transparency.

We have also added a degree of flexibility for loans and equity offering, where the capped levels of turnover have been expressed, where appropriate. These are now designed to be indicative rather than absolute. The Scheme Manager will have an element of discretion to exercise in relation to the levels of support.

The overall Scheme's aim has not changed, with the Scheme aiming to contribute activity to support the creation of between 500-1000 jobs annually over the medium to long term.

The Department of Economic Development would like to thank all those who have contributed to the Consultation and their responses have proved effective to re-designing the final scheme which will be laid before Tynwald.

Department of Economic Development, October 2015




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