

7. TAX CERTIFICATES

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i) Legislative Requirement for Certificate and Its Effect

- 7.1 In the earlier section which explained the legislation¹ it is seen that, so far as the Incentive Allowance is concerned, the requirement for certificates came only with the Income Tax (Capital Relief) (Tourist Business Incentive Allowance) (Amendment) Order 1992 (the 1992 Order). As also earlier explained,² this Order was approved by Tynwald on 23rd January 1993 and had retrospective effect with regard to events after 5th April 1992.
- 7.2 Article 2, paragraph (c) (ii) of the 1992 Order amended article 6 of the Income Tax (Capital Relief) (Tourist Business Incentive Allowance) Order 1991 (the 1991 Order) by inserting a new requirement for certificates from the Department of Tourism that the giving of relief would provide three identified economic benefits. Those benefits are set out in paragraph 5.40 above.
- 7.3 It is unclear as to why the earlier (1991) Order with which we are concerned did not have this requirement. The requirement does, however, seem to have had its origin in section 2A of the Income Tax Act 1970.³ The contemporary (September 1992) reason given for this requirement by Mr Kelly was to limit tourist business incentive allowances to approved projects only.⁴ Logically this reasoning should have applied to tourist business incentive allowances under the 1991 Order as well, but was not initially so applied. This position was rectified by

¹ Section 5

² Paragraph 5.36 above

³ File I page 253 and evidence of Mr Kelly Transcript Day 32 page 117

⁴ File I page 253

the 1992 Order by way of amendment (referred to in the preceding paragraph) to the 1991 Order which otherwise remained in force. Logically the reason for the requirement of certificates should further also have been applied to the Income Tax (Capital Relief) (Tourist Business) Order 1990 (the 1990 Order) given the continuing requirements in that Order for any aspiring beneficiary under the Order to comply with the definitions of “tourist business” and “tourist premises”, but there was not there a requirement for certificates. This last point is however probably of little significance.

- 7.4 Prior to the 1992 Order the only qualifying scrutiny for receiving tax benefits from tourism activities was the necessity for the premises to be registered under the Tourist Premises Act 1975.
- 7.5 Returning to the origins of the certification procedure coming in as a requirement under the 1992 Order, there is a material difference between the legislative requirements of the Income Tax Act 1970 and the 1992 Order. Although the wording of the three requirements in both is very similar, the bodies which have to be satisfied are different.
- 7.6 Under section 2A (i) of the Income Tax Act 1970 it is the Treasury who have to be satisfied that its own exercise of temporary tax exemption meets the three requirements; although there has to be consultation with the Department of Trade and Industry, there is no certification procedure. No doubt the Treasury would be rigorous in allowing exemptions.
- 7.7 By contrast, under the 1992 Order a department different from the Treasury (i.e. Tourism) has to do the certification, and no tests for the meeting of the three requirements referred to in paragraph 7.2 above are identified. However it appears from the wording of the 1992 Order that the relief still remains discretionary, presumably such discretion being with the Treasury, even though a certificate is granted by the Department of Tourism. Nevertheless in practice it might not be easy to exercise discretion to refuse relief, reasonably, as is required by the courts, if a certificate has been issued by the Department of Tourism. It would be unsurprising therefore if the Treasury was anxious, as

turned out to be the case, that certificates should be issued with due thought and investigation, particularly when there were no given guidelines accompanying the introduction of the certification in the 1992 Order.

7.8 Why there were no such guidelines is unclear, particularly when there were some quite rigorous requirements under other, virtually contemporary, schemes providing grant financial assistance to the tourist industry. Thus, by way of example, the Tourism Development Fund Scheme 1991,⁵ approved by Tynwald in June 1991, and amended, as approved by Tynwald in November 1992, and so quite contemporary with the 1992 Order, required under its paragraph 4 (2) information including a detailed business plan covering five years, a cash flow forecast, sources and application of funding and a marketing plan, as well as detailed specification, a bill of quantities if the total cost were to exceed £250,000, at least two quotations or tenders from approved government contractors and sub contractors, and audited accounts. Additionally, by paragraph 3 (3) assistance was prohibited where the total assistance under the scheme would exceed £50,000 in any period of two years unless the Treasury concurred in this assistance. Furthermore, not only did the Department of Tourism have to liaise with the Treasury, but by paragraph 5 (2) of the Scheme was also prohibited from approving an application for financial assistance under the Scheme unless the Department of Tourism was satisfied as to the financial viability of the project, the proposed quality of the finished product and the management ability of the operator. Yet the eligible projects specified in the Scheme⁶ were generally likely to be of a comparatively low cost order compared to a project such as Mount Murray for whom the Order which introduced the certification procedure was primarily brought into force. Mr Martin Caley described the average grant as tiny.⁷

7.9 It has been suggested that the reason there was such rigour was that grants, such as grants under the Scheme just discussed, meant that money was actually passing from the government to the grantee, and that particular care needed to

⁵ Document C80

⁶ See Appendix 1 of original Scheme and as amended

⁷ Evidence of Mr Caley Q65 Transcript Day 41 page 59

be taken, because if, for example, the grantee foundered or in some way became insolvent then the government may not recover the money.⁸ This is perfectly understandable, but is no reason at all why similar rigour should not be applied to tax reliefs, such as the tourism incentive allowance under the 1991 and 1992 Orders, and every reason why they should, given the very large amounts of relief which might be involved. Mr Kelly told us that he, as a matter of factual practice, would not make any distinction in applying the grant or the allowances system if he were responsible for issue of the certificates.⁹ We have no difficulty at all in accepting this, but everyone with this responsibility is unlikely to follow suit. We prefer the approach of Mr Caley. Mr Caley, then Senior Economic Assistant from the Economic Affairs Division of the Treasury agreed that it would have been prudent to have required similar checks as are in the Tourist Development Fund Scheme for the tax relief certificates under the 1991 and 1992 Orders.¹⁰ He was unable to say why they were not required in the legislation.¹¹ The Commission itself agrees that it would have been prudent and should have been done, given the very large sums which might be the subject of tax relief.

- 7.10 There is a further factor of contextual relevance. The wording of the 1991 Order, as now amended by the 1992 Order, indicates that the tax relief only becomes available when relevant expenditure is incurred, but the certificate may be issued at any stage, once the issuing authority, the Department of Tourism, is satisfied about the three qualifying factors. Furthermore the wording of the second requirement for the certificate, that the giving of the relief is necessary for the purpose of establishing or developing a tourist business in the Island (Commission's emphasis), properly construed, does require a full understanding of the project before the certificate can be issued, i.e. the giving of the relief is what has to be established as necessary for the purpose of establishing or developing a tourist business. If the establishing or developing of the business would happen even if there were not relief, then the criterion is not met. The proper understanding of the matter in question should not, and indeed could not, reasonably be satisfied by superficial assertions. We consider in more detail in

⁸ Evidence of Mr Gelling Q23 Transcript Day 43 page 20

⁹ Evidence of Mr Kelly Q18 Transcript Day 42 page 38

¹⁰ Evidence of Mr Caley Q65 Transcript Day 41 page 8

sub section 7 (iii) below the issue of the necessity for the proper understanding of the tourism projects in respect of which certification is being sought by developers.

ii) **The Issue of Certificates in respect of the Hotel and Hotel Extension**

7.11 The issue of the certificates was swift. As noted at paragraph 5.36 above the 1992 Order was made on 23rd December 1992 and approved by Tynwald on 20th January 1993. On 21st December 1992 the Minister for Tourism, Mr Bell, issued a certificate under the draft Order.¹² The certificate was drafted by Mr Spence in correspondence with Mr Mitchell,¹³ the Department of Tourism official in charge who dealt with these certificates,¹⁴ and initially sought to include the housing sites but, it was stated,¹⁵ in the light of the minister's concern about the villas being included the housing sites were excluded. It should be particularly noted that this certificate was signed by Mr Bell even before the Order which introduced the certificate procedure had been made in Treasury let alone approved by Tynwald and notwithstanding the letter¹⁶ which the Assessor wrote to Mr Nugent on 10th September 1992 that no written assurances could be given until the amended Order had been approved. This is remarkable. There does not appear to have been Treasury concern about the issue of this certificate.

7.12 On 26th February 1993¹⁷ Mr Nugent wrote to Mr Bell enclosing a draft certificate for an intended 62 bedroom hotel extension and multi sports hall facility, stating that he would be obliged if Mr Bell would send it to the Assessor. Mr Bell, on 2nd March 1993, did, again in identical terms to this draft, issue a certificate under the 1992 Order in respect of this hotel extension and sports hall.¹⁸ The housing sites were again excluded. There does not appear to have been Treasury concern about this certificate either, or indeed much recorded discussion, if any.

¹¹ Evidence of Mr Caley Q65 Transcript Day 41 page 8

¹² File I page 279

¹³ File I page 275

¹⁴ Evidence of Mr Toohey Q10 Transcript Day 34 pages 66 & 68

¹⁵ File I page 275

¹⁶ File I page 252

¹⁷ File I page 315

¹⁸ File I page 317

- 7.13 It is odd that certificates were being issued on directions from, and as drafted by, the recipients of the certificates. It is even more odd, and, as stated, remarkable, that the minister was prepared to sign the first of these certificates before Treasury had made the Order under which it was issued and approximately a month before Tynwald approved the Order. Ill judged unauthorised steps to support the Mount Murray development as requested is demonstrated. Mr Bell comments on this matter in a letter (response) written by him on 4th May 2004, and to which we refer in section 8. The Commission does not find that that comment particularly affects the point made in this paragraph.
- 7.14 Perhaps this is an indicator as to whether or not the Department of Tourism, the then relevant department of government, was by this stage at all in control of what was happening with regard to matters concerning Mount Murray. It should also be noted that with respect to the above two certificates no requests were made by the Department of Tourism for substantive information such as a business or marketing plan.¹⁹ It appears from the evidence that very little, if any, examination was made by the Department of Tourism as to whether or not the necessary statutory requirements for the certificate were met. There appears simply to have been the facile assumption that because the application concerned an hotel then the certificate should have been granted virtually automatically. This is an incorrect approach, as can be seen from paragraph 7.10 above, and from the evidence that the hotel project would in any event likely have proceeded without the benefit of these new tourist business incentive allowances (see paragraph 6.43 above). Failure to give due consideration provided Mount Murray with the availability of very substantial amounts of tax relief (many millions) without any of the testing which the legislation required. We deal with appropriate requirements in the next following sub section.

¹⁹ Evidence of Mr Toohey Transcript Day 34 pages 66 & 68

iii) **Certificate for Housing**

- 7.15 Things were very different when the developer sought to obtain tourist business incentive allowance certificates in respect of housing. The vigour with which the developer fought for these certificates was considerable and really belies the simplistic assertions and statements that no claims were made for tourist business incentive allowance relief in respect of housing.²⁰ The developer tried very hard but did not succeed in achieving even the first requirement of obtaining certificates for the majority of the housing sites, thanks mainly to the approach of the Treasury, and because of a change of business plan²¹ whereby they appeared to go for full residential use. Nevertheless they did get a document related to the housing, referred to below, which was not a certificate but which they utilised for marketing purposes²² in the sale of the housing sites.
- 7.16 The housing certificates dispute really started with a letter from Mr Spence to Mr Bell dated 9th September 1994.²³ The letter stated that planning permission for the villas had been extended until 1999 and serious marketing was to start. The tourist business incentive allowance was to be a valuable marketing tool and confirmation was requested that “provided investors offer the villas or apartments for six months of the year and register with the Tourist Board ... then they would receive the benefit of the tourist business incentive allowance in respect of the cost of the building.” The marketing purpose was frequently reiterated by the developer.²⁴
- 7.17 On 20th September 1994 a fax was sent to Mr Toohey by Mr Spence. This comprised a draft certificate to the effect that all the housing land (known as Phase II of the Mount Murray development) qualified for relief under the 1992 Order. The last sentence stated “For further clarification we would confirm that the above view (of qualification) is on the understanding that individual houses will be registered as tourist premises and that tourist business will be carried out

²⁰ Mr Gough's question to Mr Kelly: Evidence of Mr Kelly Q18 Transcript Day 33 page 98

²¹ File II pages 364 & 365 note of meeting 14.10.1994

²² File II page 516 7.2.1995

²³ File II page 322

²⁴ File II pages 322 to 515: correspondence between September 1994 and February 1995

from these premises.” This fax was endorsed by Mr Spence as having been drafted by Mr Nugent. Mr Nugent did not dispute this endorsement.

7.18 Without any delay Mr Toohey sent a letter, dated the following day, 21st September 1994, to the Assessor, Mr Kelly, which was in effect in the terms of the ‘certificate’ said to be drafted by Mr Nugent, but it had a final paragraph in the following terms. “I should be pleased if you could ensure that this matter is treated with the utmost urgency and that the company is given an early decision.”²⁵ This does not appear to be an appropriate sentence if this letter was only a draft for approval. However Mr Toohey claimed that this was a draft letter²⁶ and a copy of it has an endorsement by Mr Toohey that this is the case. It is however unlikely that this was a contemporary endorsement as the letter was signed by Mr Toohey's deputy as Mr Toohey was away when the letter was sent and Mr Toohey agrees that it was not contemporary.²⁷

7.19 Mr Toohey denies most strongly that he believed when he issued this document dated 21st September 1994 that he was indeed issuing a certificate.²⁸ We disagree. We find contemporary documents to be persuasive that he did so believe. Mr Toohey explained that when the document was issued he was away and a colleague inadvertently omitted to mark the letter as a draft, and inadvertently included within the body of the letter Mr Toohey's request that there be early comment from the Income Tax Division. He reiterated that the document simply was in draft form for comment and advice.²⁹ These may well be Mr Toohey's recollections but correspondence and memoranda indicate otherwise. Treasury appear to have thought that a certificate had been issued.³⁰ Most importantly Mr Toohey wrote to Mr Spence on 30th September 1994³¹ confirming that a letter had been forwarded to Treasury "in support of the TBIA". He said that he was waiting for Treasury permission before sending Mr Spence

²⁵ File II page 330

²⁶ Evidence of Mr Toohey Q10 Transcript Day 34 page 79 seq

²⁷ Evidence of Mr Toohey Q10 Transcript Day 44 page 26 and Letter Mr Toohey 23.4.2004 page 2 Annex 9

²⁸ Letter Mr Toohey 23.4.2004 page 2 Annex 9

²⁹ Letter Mr Toohey 23.4.2004 pages 2 & 3 Annex 9

³⁰ File II pages 331 & 332 Treasury Internal Memos 26 & 28.9.1994

³¹ File II page 335

that letter of support. The Commission has seen no document which might be described as a "letter of support" other than the material letter of 21st September 1994. Mr Toohey then went on to describe what he perceived was the tourist business incentive allowance system. He said "... it is the Income Tax Division of Treasury that has the issuing authority in respect of such a scheme. This Department merely provides support documentation to the Income Tax Division which it has done". The fact of the matter is that the legislation procedure in question does not make provision for support documentation other than by issue of a certificate, which can be regarded as a support document, though more accurately it would be a prerequisite or qualifying document. His letter of 30th September 1994 specifically confirms that such a document was issued. This 30th September 1994 letter is in response to an earlier letter of 29th September 1994³² from Mr Spence, who wrote that Mr Toohey had confirmed that a certificate had been issued and had indicated that a copy would be sent to Mr Spence. The letter of 30th September 1994 not only does not deny these matters, but is really quite consistent in that it says "I would confirm again that a letter [of support has been forwarded to Treasury]." The point is further confirmed by the next two following letters. Mr Spence responded³³ by expressing surprise that as a Chief Executive with authority to issue a certificate he needed Treasury consent from a lower ranking officer and stated, as he had done in an earlier letter,³⁴ that Mr Toohey had told Mr Spence that he had issued a certificate. Mr Toohey replied the same day but did not deny what was claimed as to the issue of a certificate. Mr Toohey does not accept that these matters show that he believed he was issuing a certificate, but we find that these are really quite conclusive that, so far as he understood the certificate legislation, Mr Toohey issued a document which he believed was required by it.

7.20 Furthermore Mr Toohey informed the Attorney General on 14th October 1994 that the reason that the housing sites were excluded from the certificate issued on 21st December 1992 was in order to satisfy the Department of Tourism's "concern that the hotel and leisure complex phase of the development should be

³² File II page 333

³³ File II page 336

³⁴ File II page 333

completed before the residential housing phase began".³⁵ This reason clearly had nothing to do with the statutory requirements for issuing or not issuing certificates and had effectively been overcome by late 1994. The true situation appears to be that Mr Toohey did not really understand the certification procedures when he wrote the letter of 21st September 1994. In any event, although it does have the appearance of a certificate, a close examination of external circumstances would show it not to be a valid certificate because it did not meet all necessary requirements.³⁶ We say more about Mr Toohey in section 8 below, and he has written a letter in response³⁷ to which we also refer in section 8.

- 7.21 There was concern in the Treasury about this matter. Treasury was not aware of all the facts about the development and, the Assessor and the Chief Financial Officer having discussed the matter on 26th September 1992, Mr Toohey was to be advised not to issue the certificate.³⁸ It became the subject matter of bitter correspondence from the developer, including threats of litigation. We have referred to the start of that correspondence at paragraph 7.19 above.
- 7.22 Treasury advised Mr Toohey by letter dated 30th September 1994 that he was endeavouring to advance matters a little ahead of what was possible, indicated that full consideration of Phase II (the housing proposals) was never fully embarked upon, and a meeting was suggested in order to identify relevant information required from the developer. Correspondence continued to come from the developer at a rapid rate.
- 7.23 On 4th October 1994 Mr Spence wrote to the Chief Minister, the Minister for Tourism and the Treasury Minister.³⁹ The letters complained that a certificate had been issued (the 21st September 1994 letter), that it had not been released to the developer, that this was entirely a matter for the Department of Tourism, that the Treasury was acting unlawfully in interfering with the issue of a

³⁵ File II page 370

³⁶ File II page 362 point 3 and page 467

³⁷ Letter Mr Toohey 23.4.2004 page 2 - see Annex 8

³⁸ File II page 331

³⁹ File II pages 338 seq

certificate, that marketing was being held up, that serious economic damage would follow, and that personal intervention from all three ministers was required. On the same date Mr Nugent wrote to the Deputy Assessor in more measured tones but effectively making the same basic point that it was for the Department of Tourism to decide whether the criteria under the 1992 Order were met or not.

- 7.24 Correspondence still continued; Treasury explaining to Tourism that they (Treasury) were not restricting the issue of a certificate but were seeking more information with further reference to a meeting, and Mr Spence demanding that a certificate be issued “by noon tomorrow” or give good reason why not.⁴⁰
- 7.25 A meeting did take place on 13th October 1994 between Messrs Spence, Nugent, Toohey, Kennaugh (Deputy Assessor) and Caley (Senior Economic Assistant at the Treasury, whose role was to offer advice to the Department of Tourism as to the economics of the matter⁴¹). There are two full notes of that meeting.⁴² One made by Mr Kennaugh and the other by Mr Caley. Mr Kennaugh noted that the meeting in the main constituted Mr Spence contending that a certificate for tourist business incentive allowance had been issued and that he was going to have to see the Chief Minister if it was not handed over. He was dissuaded from this course and it was noted that ultimately Messrs Spence and Nugent agreed to provide relevant particulars to the tax and tourism authorities so that the underlying base could be confirmed and the issue of a certificate appraised.
- 7.26 Mr Caley’s note is much more detailed. It covers the same basic ground, but does include a few points of detail which are worth bringing to attention. First, the developer contended that a gentleman’s agreement existed, made with Mr Bell, the former Minister for Tourism, that there would be no problem with the certificate for Phase II. We should say here that we asked Mr Bell about such agreement and he said that the claim was nonsense.⁴³ We have seen no evidence to justify the claim that there was such agreement. Second, the developer contended that Phase I was not viable without Phase II which itself

⁴⁰ File II page 359

⁴¹ File II page 363

⁴² File II pages 362 and 364

depended upon the availability of tourist business incentive allowances for Phase II. Third, the meeting was informed that Phase I occupancy was doing better than expected and the original business plan, presumably showing the inter-phase dependence for viability had been scrapped, and not replaced. Fourth, that Treasury understood that the Phase II planning permission restricted its usage to tourism with restriction on occupancy. This error was a result of misinformation supplied by Mr Brian Sinden of the Department of Local Government and the Environment, who accepts that he did misinform Treasury in this way.⁴⁴ Fifth, that Treasury would be looking at the company's business plan and its associated marketing plan to assess its potential for getting new business. A letter was to be drafted setting out Treasury's requirements, and we refer to this below. Sixth, the Attorney General was to be consulted upon whether the letter of 21st September 1992 was, or was not, in fact a certificate.

7.27 On the following day, 14th October 1994, the letter just referred to, the draft of which had been agreed by Mr Caley,⁴⁵ was sent to Mr Spence by Mr Toohey requesting information to progress the request for a tourist business incentive certificate.⁴⁶ It was a thorough and searching request. It sought a business plan which was to include incorporating estimated annual numbers of visitors, estimated annual bednights and total visitor spend. A copy of the marketing plan to achieve the business plan was also sought, as was an estimate of projected employees and the basis of the full letting programme in respect of the scheme. It asked for notice of any other factors related to the scheme which were clearly in the interests of the economy of the Island. It noted that there would be other questions or concerns and, in the interim, sought written answers to the matters specified in the letter.

7.28 The letter was never replied to,⁴⁷ and the totality of the evidence before the Commission indicates that the information requested has never been received by

⁴³ Evidence of Mr Bell Q9 Transcript Day 36 pages 98 & 99

⁴⁴ Mr Sinden Q12 Letter 6.1.2004

⁴⁵ File II page 365

⁴⁶ File II page 369

⁴⁷ Evidence of Mr Caley Q65 Transcript Day 41 pages 60 & 61

government. But, by the 19th October 1994,⁴⁸ Mr Spence was writing a detailed letter to the Chief Minister referring further to unauthorised interference by the Treasury, describing all government's behaviour as disgraceful, and referring to the investment of many millions of pounds. A request was made for personal intervention with directions to be given to the two ministers concerned, reference was made again to serious economic loss, and the final words were a reference to litigation. On 28th October 1994 Mr Spence wrote further to the Chief Minister stating that if there were not assurances within one week that the certificate would be released, then application would be made to the High Court. The threat was repeated in a letter of 4th November 1994 which contained further complaints.

- 7.29 In a memo to the Treasury Minister dated 31st October 1994, Mr Kennaugh noted that the Attorney General had advised that expenditure had to be incurred before a certificate could be issued. This opinion was expressed in the Chief Minister's response to Mr Spence dated 4th November 1994 which stated that, as referred to in paragraph 7.28 above, further information was awaited by government before the matter could be progressed, and that the appropriate way forward was for that information to be provided. Mr Spence nevertheless persisted in his correspondence to the Chief Minister and the threats of litigation with letters dated 8th, 15th and 21st November 1994.
- 7.30 Following advice from the Attorney General the Chief Minister wrote again to Mr Spence on 24th November 1994 explaining that the Treasury was the government department with prime responsibility for the administration of the capital relief system, and, further, reiterated that the matter could not be further progressed until the Treasury and Department of Tourism had received all the information requested.
- 7.31 Mr Spence responded on the same day, claiming that the Chief Minister had agreed the points he had made, that there was already in existence a forward commitment from the Department of Tourism to register the houses as tourist

⁴⁸ File II page 372

premises, referring to a letter from Mr Toohey to Mr Kelly dated 3rd June 1992 and saying that he would not give the particulars requested, as they would only arise if a purchaser from Mount Murray actually applied for tourist business incentive allowance relief, and it would be the particulars of that applicant, not of Mount Murray, which would be material; the request for the 'certificate' of 21st September 1994 was repeated.

7.32 The Chief Minister responded on 28th November 1994 with a letter suggesting that information was being sought to see whether a certificate could be issued in advance of completion and suggesting a meeting with officers of the two concerned departments. Mr Spence responded the following day with a detailed explanation of why the certificate should be issued and again requesting the 'certificate' of 21st September 1994, otherwise legal proceedings would be issued at the end of the week, on the 2nd December 1994. The Chief Minister acknowledged this letter on 2nd December 1994 and reiterated his position.

7.33 Mr Spence responded this time by requesting a meeting. A meeting was arranged for 8th December 1994 on a without prejudice basis between government and its legal advisors and the developer and its legal advisors. Later in December, and in January 1995, draft 'certificates' were produced and commented upon by both parties. Further meetings took place in January. Ultimately on 16th January 1995 Mr Toohey wrote a letter, accompanied by a plan, which did satisfy the Mount Murray developer. This letter had been agreed between the parties and their legal advisors at meetings between the parties prior to that date.⁴⁹ It was in fact little more than a letter of intent or comfort which set out the requirements of the law with regard to the issue of certificates, and how those requirements would be complied with. It appears clearly enough that it was in fact accepted by the Mount Murray legal representatives that the letter of 16th January 1995 would be by way of a statement of intent which relates to considerations which would be given by the Department of Tourism in respect of any application.⁵⁰ Mr Kennaugh emphatically rejected any suggestion that it

⁴⁹ File II page 515

⁵⁰ File II page 467

was a certificate or had ever been regarded by the Income Tax Division as a certificate for houses at Mount Murray.⁵¹

7.34 It should be noted however that, in contrast to the rigour of the letter of 14th October 1994 (see paragraph 7.27 above) it does seem to have accepted, without much apparent scrutiny, that the statutory certification criteria would be met if the two government departments of Tourism and Treasury were satisfied about other matters. No answer to that letter of 14th October 1994 had been received, nor otherwise had the requested information been supplied, as explained in paragraph 7.28 above. It can only be assumed that under the pressure of threats of litigation and anxiety to reach some element of settlement with the developer government overlooked the importance of what had been decided on 13th October 1994 as to what was required before a certificate could be issued. Indeed the letter of 16th January 1995 contradicts the reasoning, advice and decisions of the meeting of 14th October 1994. Nevertheless it is clear from the documents that Mr Toohey and Mr Kennaugh had been fully involved in the negotiations leading up to the letter and had approved a draft of it.⁵²

7.35 Mr Willers referred to the letter of 16th January 1995 in evidence and correspondence to the Commission.⁵³ In earlier oral evidence he had told the Commission that in order to benefit from the tourist business incentive allowance the area in question had to be designated by the Department of Tourism.

7.36 He had also said that he had a plan which had the whole of the area zoned, and that one could only get a tourist business incentive allowance if one fell within a designated area; that designation meant a certificate issued; that a certificate was vital and that without a certificate the housing could never have been made available by people paying for them as holiday homes because there was no incentive to do it, and in the actuality it turned out that nobody was incentivised anyway; that a certificate (the letter and plan of 16th January 1995) was issued

⁵¹ Evidence of Mr Kennaugh Q54 Transcript Day 39 pages 73 - 75

⁵² File II pages 487, 488 et seq, 502, 503, 506

⁵³ Evidence of Mr Willers Q2 Transcript Day 37 pages 72 - 76 and Letter 14.11.2003 with enclosures

for all the housing at Mount Murray; that the correspondence, which we have described above and included threats of court action, had the purpose of obtaining what he claimed was the certificate; and that the housing was marketed with the benefit of the tourist business incentive allowance.

7.37 This explanation is a helpful indicator of the relationship between housing and tax because on 7th February 1995 Mr Spence was writing⁵⁴ to the Chief Minister expressing appreciation for his intervention, explaining that the letter of 16th January 1995 would prove a valuable marketing tool, and enclosing a draft of an advertisement⁵⁵ for sale of fully serviced plots on the "Island's first ever Golf Course Residential Development" which had in its heading the claim "The Ultimate Luxury Living for Permanent Residents". The advertisement explained that the planning authority had already approved 25 different housing styles designed for permanent residents, but made reference to the 250% tax relief scheme as an additional attraction in appropriate circumstances. This draft advertisement also shows that Mr Willers was incorrect when he did not accept⁵⁶ that if no certificate had been issued an option would have been to market the houses as permanent homes, because almost immediately after the issue of what appeared to be a certificate (but was not) the plots were being advertised primarily for permanent residents, but, within the advertisement, using the "valuable marketing tool" of reference to the 250% tax relief.

7.38 Mr Willers helpfully supplied the Commission with a copy of the letter of 16th January 1995 together with an accompanying plan upon which housing proposals were edged red. The letter and plan of 16th January, in this respect, is a geographical identification of the Phase II (housing) element of the Mount Murray development. As the letter points out "Phase 2 means those housing sites which form part of the Mount Murray tourist development at Santon, Isle of Man, edged red on the attached plan."

⁵⁴ File II page 515

⁵⁵ File II page 517

⁵⁶ Evidence of Mr Willers Q2 Transcript Day 37 page 81

- 7.39 This latter information has limited relevance as to whether a certificate could or should be issued other than a pragmatic confirmation of the exclusion of certain areas of land from the hotel related certificates as referred to in paragraphs 7.11 and 7.12 above. However while it is certainly not a certificate, and leaves a lot of matters to be established by the certificate applicant, it does, as noted in paragraph 7.34 above, indicate that if these matters are established the certification criteria would be met even though the Department of Tourism did not have information which would have enabled them properly to make that judgement.
- 7.40 The account of events leading up to the letter of 16th January 1995 has been set out in detailed form in order to illustrate the determination of the developer in seeking to achieve, and in achieving, what it required, and to illustrate how government reacted to this particular instance of persistence and pressure. It did not react very well. The Department of Tourism Chief Executive, Mr Toohey, did not seem to understand the certification procedures. Matters were put back on track by taking and acting upon sound advice from the Treasury, but that advice was overlooked under the continued pressure being exerted by the developer.
- 7.41 On 9th February 1995 Mr Spence made a formal request⁵⁷ to Mr Toohey for a certificate to be issued under the 1992 Order in respect of 23 houses within Phase II of the Mount Murray development, again accompanied by a draft certificate. This letter contended that the Department of Tourism and Treasury had confirmed that certificates would be available for the housing Phase II. Those departments had not in fact so confirmed unless in any particular case they were satisfied that the relevant statutory requirements had been met.
- 7.42 Internal discussions with government took place with a resultant delay which led to Mr Spence again threatening legal action. A request for information, on advice, was sent by Mr Toohey on 27th March⁵⁸ and a response was received on 28th March 1995.⁵⁹ Unfortunately, while the request referred to a number of

⁵⁷ File II page 518

⁵⁸ File II page 548

⁵⁹ File II page 550

procedural matters, it asked for no information at all with regard to the substantive economic criteria as to whether a certificate under the 1992 Order was merited on the basis of those statutory criteria. The reply from Mount Murray Country Club Limited provided all the information requested and was accompanied by a threat that unless the certificate was issued the following day then there would be adverse comment in the Financial Times about the government's attitude to tourism, reflecting the government's positive hostility to further investment in tourism at Mount Murray and its refusal to act as required by law. This letter was copied by the developer to the Chief Minister. Threats of legal proceedings continued over the next few days, together with further threats about the Financial Times, unless the certificate was issued.

- 7.43 On 4th April 1995 the Attorney General wrote a quite detailed explanatory letter⁶⁰ to the developer's advocate seeking further information, following receipt of which it was said that the application would be given consideration. The Attorney General assured the developer's advocate that the Department of Tourism was supportive of tourist development in the Isle of Man.
- 7.44 Whilst the letter was detailed in form, a significant part of it sought confirmation of information which had been supplied by the developer in the 28th March 1995 letter, and the Attorney General recognised that in his letter. However the letter did specifically refer to article 6 (3) (b) of the amended 1991 Order and asked for confirmation that "the giving of relief in respect of the Tourist Business of the Company to which the relief relates is necessary for the purpose of developing the Company's Tourist Business in the Island."⁶¹ Unsurprisingly the answer, received the same day, was the single word "confirmed".⁶² The question posed is in remarkable contrast to the letter of 14th October 1994 (paragraph 7.27 above) which was directed to the same issue but was very much more meaningful. On the basis of this virtually non-existent information a certificate was issued on 10th April 1995 certifying that the three statutory economic criteria

⁶⁰ File II page 593

⁶¹ File II page 594

⁶² File II page 590

had been met. The rigour of the 13th and 14th October 1994 had been abandoned again, no doubt because of the pressure applied by the developer.

7.45 Mr Caley was asked about these matters and provided some valuable factual background and opinion. He explained that the tax position was relevant to the making of grants and loans in terms of a wider economic appraisal about the benefits of tourism, or a new tourism project, to the economy; that if all that is happening is a diversion from existing businesses it is not worth any money to the government or the economy. It is required to see, if a grant is given, whether the grant is going to come back into revenue, partly by direct tax but also by indirect tax such as VAT and duty taxes.⁶³ He thought it would be prudent that if a certificate was required as a prerequisite for tax relief, as under the amended 1991 Order, documents of a similar kind to those required under a grant scheme (see paragraph 7.8 above) should also be required to support such tax certificate application, even though the legislation does not expressly require it.⁶⁴ He also explained⁶⁵ in some detail and with good reasoning why the detail requested in the letter of 14th October 1994 was required. These reasons included the point that for a tourist project to be worthwhile to the Island it would be required to show that it had the potential to attract new visitors,⁶⁶ and the requirement that part of the consideration for a certificate would involve an assessment of the potential loss of tax revenue.⁶⁷

7.46 He also said that he would have expected to have been involved in the letter of 16th January 1995, but that he was not.⁶⁸ Mr Caley was after all advising the Department of Tourism on economic matters, which certification was primarily about. He said that he had advised that certain information should be requested, and he never saw that information, surmising that his advice was rejected.⁶⁹ He further told us that he had no involvement in the issue of the 10th April 1995 certificate, but would have expected to have been involved for the same

⁶³ Evidence of Mr Caley Q65 Transcript Day 41 pages 5 & 6

⁶⁴ Evidence of Mr Caley Q65 Transcript Day 41 pages 8 & 11

⁶⁵ Evidence of Mr Caley Q65 Transcript Day 41 page 35 seq

⁶⁶ evidence of Mr Caley Q65 Transcript Day 41 page 37

⁶⁷ Evidence of Mr Caley Q65 Transcript Day 41 page 42

⁶⁸ Evidence of Mr Caley Q65 Transcript Day 41 page 55

⁶⁹ Evidence of Mr Caley Q65 Transcript Day 41 page 55

reasons.⁷⁰ He added that if he had been involved with its issue he would have asked to see the response to the request for a business plan; and went so far as to say that he would ask for this because he had no information at all about whether such a certificate should be issued. Again his advice appears to have been ignored. Indeed he had not seen the 10th April 1995 certificate until he gave evidence to us.⁷¹ We find this to be a quite remarkable state of affairs which the government had allowed itself to adopt under pressure from the developer.

7.47 Mr Kennaugh was also asked⁷² about this certificate of 10th April 1995. He thought that it was certainly a bit odd, he was at a loss over it, it was not on his files and he had never seen it before this Inquiry. He said that if Mr Toohey had issued it he had a feeling that he would have been speaking on the phone to him straight away. Although Mr Kennaugh used fairly robust terminology it is an illuminating comment which we set out verbatim, and may illustrate how the government tended to depart from its general approach when under pressure. "In fact, after all the trouble that was taken with the AG to determine that a certificate could not be given, that effectively the buildings had to be in existence, the expenditure had to have been incurred, etc, etc, etc and that only a letter of comfort could be given until that time, my own view is that, if I was to have received that, my immediate reaction would have been 'How the hell has this happened in the light of what's gone on before.'"⁷³

7.48 However, although this may appear a reasonable comment from an objective third party observer, the fact is that, as with the issue of the letter of 16th January 1995, Mr Kennaugh had been fully involved by the Attorney General in the discussions and provision of instructions to the Attorney General before the certificate of 10th April 1995 was issued. Specifically Mr Kennaugh was invited to comment and to suggest amendment to the Attorney General's letter of 4th April 1995 (see paragraphs 7.43 - 7.44 above).⁷⁴ He gave specific approval to the

⁷⁰ Evidence of Mr Caley Q65 Transcript Day 41 page 56

⁷¹ Evidence of Mr Caley Q65 Transcript Day 41 pages 60 & 61

⁷² Evidence of Mr Kennaugh Q54 Transcript Day 39 pages 75 - 78

⁷³ Evidence of Mr Kennaugh Q54 Transcript Day 39 page 77

⁷⁴ File II page 575

draft.⁷⁵ While this letter was not, of course, the certificate, he must have been well aware, because of his involvement with events relating to that certificate, that the issue of the certificate was likely to follow closely once the answers were provided by the applicant. It is also the fact that the Attorney General suggested⁷⁶ to Mr Toohey that any draft certificate might be provided to Mr Kennaugh to ensure his satisfaction with it. Whether or not he was so provided is unclear from the papers, but, whether he received it or not, the certificate followed the format of the letter of 4th April 1995 closely, and there was no departure from the thinking which had been demonstrated in the letter of 4th April which he had approved. It is not easy to explain this apparent contradiction on the part of Mr Kennaugh, but we have no reason or evidence to indicate anything untoward in Mr Kennaugh's conduct. Mr Kennaugh has responded to this paragraph by letter set out in Annex 9. He is not able to explain the contradiction but reaffirms the essence of his view. He does refer to the submission of his Advocate relating to the issue of certificates. We have addressed these matters elsewhere, but they do not bear upon the apparent contradiction.

- 7.49 In any event, as indicated, on 10th April 1995 the certificate was issued by the Department of Tourism under the 1992 Order in respect of the 23 houses. They had not at that stage been registered as tourist premises, (nor so far as the Commission is aware have they ever been so registered).
- 7.50 We have in this section referred to Mr Toohey in critical terms and refer to this further in section 8, but the criticism needs to be understood against the difficult departmental background within which he was operating. Although he was Chief Executive of the Department of Tourism, the certificates issued in respect of the hotel and its extension were dealt with directly by Mr Mitchell and signed by Mr Bell.⁷⁷ Mr Toohey was not aware of the information upon which the certificates had been issued.⁷⁸ He was unaware whether a business plan, feasibility or marketing study had been seen by the Department of Tourism when the certificates were issued. Mr Toohey's answers were a little unclear at this point,

⁷⁵ File II page 584

⁷⁶ File II page 598

⁷⁷ Evidence of Mr Toohey Q10 Transcript Day 34 pages 66 - 68

but he did appear to be saying that there should have been a far more detailed requirement of information to be provided to the Department of Tourism before these certificates were issued.⁷⁹

7.51 When the time came to consider the housing certificates Mr Mitchell was not involved,⁸⁰ and Mr Toohey was directly involved with their consideration. Although the tourist business incentive allowance procedures had been by then in force for some time, they were new to Mr Toohey. We do not find that the procedures set out in the 1992 Amendment Order were particularly complicated, but we do accept that the appropriate interpretation does require clear thinking. Mr Toohey probably recognised that when he described the issue as being one which was involved and detailed.⁸¹ He was also under considerable pressure from Mr Spence and he was, rightly, concerned that he did not make mistakes in the production of the documents and produce what he described as being documents which were not going to be in the department's best interests.⁸²

7.52 It is clear from the documentation which we have⁸³ that by this stage Mr Toohey made every effort to obtain advice as to the correct procedures from all his available sources. In some cases this was accepting and listening to advice which was put to him. Ultimately because of pressures and threats from the developer, he was receiving advice from the Attorney General as to how to proceed. This advice was being given after discussions with the developer's legal representatives and detailed discussions with Mr Kennaugh under the advice of the Attorney General. So in reality Mr Toohey was receiving and seeking advice as to how to proceed on the issue of certificates from October 1994 until after the issue of the certificate on the 10th April 1995.

7.53 While we find that there is no doubt that mistakes were made as to the proper issue of these certificates, these mistakes were made by Mr Toohey when he was following advice from others notwithstanding that it turned out that that

⁷⁸ Evidence of Mr Toohey Q10 Transcript Day 34 pages 66 - 68

⁷⁹ Evidence of Mr Toohey Q10 Transcript Day 34 pages 67 & 68

⁸⁰ Evidence of Mr Toohey Q10 Transcript Day 34 page 68

⁸¹ Evidence of Mr Toohey Q10 Transcript Day 34 page 69

⁸² Evidence of Mr Toohey Q10 Transcript Day 34 pages 69 & 70

advice was conflicting advice. If, as was the case, Mr Toohey was having difficulty in appreciating the correct processes for operating this particular legislation, the tourist business incentive allowance, then he did the correct thing by seeking advice from sources which he believed to be appropriate sources as to how best to process the relevant procedures. He should not be blamed for that.

7.54 Mr Toohey put his position to us quite clearly;⁸⁴ that he didn't want the department to be a stand alone department and should not be giving out certificates without going through the process and liaising with other departments, hence him speaking to Treasury and also having the great comfort that the Attorney General in fact was present. He said it (the certificate request) had been "passed through Income Tax", and that they had had the opportunity to, and did, make plenty of comment about it prior to its production and likewise the Attorney General. He further added⁸⁵ that, being under pressure from Mr Spence, he was going to make 100% sure that he wasn't going to step into anything which was going to create major problems. He was anxious that Mr Spence should get answers which were correct answers. He hoped that he was doing it the correct way and to ensure this he was getting advice from someone in government. This was because he was still relatively new to the procedures with which he was involved.

7.55 In 1999 there was further discussion with a different developer who was considering acquiring some three or four houses at Mount Murray for tourist holiday accommodation. The issue of tourist business incentive allowance under the 1992 Order was a topic of discussion, but the possible proposal did not proceed.

7.56 Despite the very strong and lengthy pursuit of certificates for housing in Phase II matters have not proceeded beyond the issue of one certificate as explained

⁸³ File II

⁸⁴ Evidence of Mr Toohey Q10 Transcript Day 34 page 76

⁸⁵ Evidence of Mr Toohey Q10 Transcript Day 34 page 84

above, and there has been no actual making of a claim for relief under the Tourist Business Incentive Allowance Order 1991, as amended.

iv) **Later Developments with regard to Certification**

7.57 We have referred to the need for a more rigorous approach to the issue of certificates than was operated in relation to the issue of the certificates in relation to the Mount Murray development. For example we have referred to the views of Mr Caley, we have referred to how Mr Toohey had difficulty in identifying precisely what approach should be taken, and we have referred to how there were weaknesses in the issuing of the Mount Murray certificates.

7.58 These concerns appear to have been recognised at least by late 1997. This can be seen in a letter written by Mr G Le Page then, and now, Director of Tourism, on 27th October 1997⁸⁶ to Mr Kennaugh. In this letter Mr Le Page said that it had been agreed that guidelines should be produced to assist in processing future applications for tourist business incentive allowance. He referred to a meeting he had had with Mr K C McGreal, then Treasury accountant with responsibility for the Department of Tourism, in order to discuss this and that a draft would be circulated for comment. He said that these guidelines would be helpful in dealing with future claims. He also commented that it might be appropriate to consider some amendment to the current Order as all felt that the then wording may require improved interpretation. Mr Kennaugh's response⁸⁷ mainly related to other matters in Mr Le Page's letter, but he did state that the decision as to certification was for the Department of Tourism alone, having established its own benchmarks after discussion with other divisions of government whose views the Department of Tourism thought relevant in its deliberations. This is of course an accurate statement of the legal position.

7.59 We sought information as to how the draft guidelines proposed in 1997 had progressed. We asked Mr Toohey about these matters. He provided⁸⁸ us with

⁸⁶ C70

⁸⁷ C70

⁸⁸ Letter Mr Toohey 12.3.2004 & enclosures

Guideline Notes for applications for tourist business incentive allowances as prepared in 1997, and a Note of Procedures dated 25th January 2004 which explains that procedures which work well are now agreed with the Income Tax Division, and that these procedures are identified in the Note so that there has not been need to publish Guideline Notes. We were also provided with a note of guidance on economic appraisals. These must now be carried out whenever a department is proposing the introduction of a new or enhanced service. These documents show there has been an advance on the approach to introducing new procedures, operating existing ones, and interaction between government departments. We return to this in our recommendations section.

END OF SECTION 7

