



MEGA SECTOR REVIEW 2014

SUMMARY OF VIEWS RECEIVED FROM KEY MEGA MEMBERS

MARKET CONDITIONS

Currently there are three key influences on the development of egaming in the Isle of Man: the continued growth of well-established companies; the difficulty faced by start-ups and smaller companies facing uncertainties and increased barriers to entry; the new opportunities that will be created by FX, binary and cyber currency prospects. Thus while overall there is expected to be some modest growth in the sector there could be a significant boost to income and employment if any of the major prospects in these new areas come to fruition.

2013 has generally been good for the industry-leading companies headquartered on the Isle of Man, bringing new activities and associated companies here. The global gaming market itself appears to have stagnated in some areas but mobile systems are enjoying significant growth.

The various changes and uncertainties outlined below lead to the expectation of an industry that is likely overall to be flat during 2014 unless there are significant contributions to income and employment from the new activities being encouraged to locate here.

Surveys show that quality of life on the Island is exceptionally high so it is not surprising that staff who have moved to the Isle of Man report that they are very happy with life here. Inevitably, a small proportion intends to return to their home country for family or personal reasons. The advantage of relocating specialist staff to the Isle of Man is that their skills are transferred to local staff so the Island's skill base is improved. When questioned about the application of work permits, companies stressed that it is essential that staff already working for a company be allowed to transfer without hindrance and that those being promoted or changing role should not need work permit approval. It is obvious that in these cases companies will not appoint any other candidate in place of their own employee, so the laudable aim of trying to protect local employees has the unfortunate consequence of actually reducing growth opportunities in such instances.

There are varied views on the amount of growth expected during 2014. Specific circumstances and activities determined the forecasts of reporting companies; some anticipate a flat year, others double-digit expansion. There is a mixed reaction to the future, with uncertainty because of UK POC tax and regulatory concerns. Overall, while a relatively "flat" year generally is anticipated it is expected that there will be some continued growth in business through 2014 with staff numbers forecast to rise by about 5%. While the e-gaming sector is likely to continue to be an important provider of excellent employment opportunities, contributor of revenue and supporter of community projects, the halcyon days of it driving rapid growth for the Island may be over, so far as existing licensees are concerned. All that could change, however, with the addition of even one

new licensee with significant employment numbers or the rapid growth of those new prospects identified above.

POTENTIAL NEW BUSINESS

While growth from existing business is expected to be steady rather than spectacular, there is a respectable pipeline of new licence applicants, although tough regulatory conditions and other barriers make entry to the e-gaming business much more expensive and tougher than in previous years. New business sectors that DED and the business sector have targeted include binary options, FX opportunities and lottery messengers which will be appropriately regulated on the Island. There is a respectable number of new applications for licences in the pipeline but there have been a few casualties with licences being surrendered by unsuccessful entities.

Those who attended ICE and other trade exhibitions have been encouraged by the quality of interest shown and it is already apparent that there are real possibilities for growth to ensue from FX, binary and crypto currencies, for example bitcoins. Recent adverse publicity surrounding crypto currencies indicates the need for the Isle of Man to consider carefully applications in these new areas and to recognise that possession of a licence could confer considerable benefit to the recipient but significant reputational risk to the Isle of Man.

It may be worth reiterating again that MeGA's view is that licence numbers alone should never be considered the sole indicator of success for the online gaming industry. Rather, quality employment and income generating opportunities should be the goal.

INDUSTRY RELEVANT ISSUES

LEGAL & REGULATORY

UK LICENSING MATTERS

UK licensing matters have taken up a great deal of time and expense, since the last quarter of 2013, for those companies heavily involved in the UK. The year ahead will be no less challenging regarding UK licensing requirements as there are uncertainties over such questions as whether a company without clients in the UK can advertise on premier boards and the shirts of British sports teams, without requiring a UK licence. Views on this are divided but the consensus is that a licence will be required and that it is certainly the Gaming Commission's desire to license every company having any gambling activity at all in the UK. The GSC confirmed its view that it anticipates the UK will require a licence even when marketing is the sole activity undertaken by a company in the UK.

There is concern that the UK GC is under-resourced and those affected would welcome even closer relations between the Isle of Man and UK regulators. It has been suggested that the Isle of Man GSC should aim to negotiate for a simple, almost automatic licence process, where Isle of

Man licences are grounds for fast-tracking when application is made for a UK licence; such arrangements between regulators are not unusual.

SHOULD GOVERNMENT LICENSE SOFTWARE DEVELOPMENT COMPANIES?

The question was posed as to whether software companies should be required to be licensed. While it may be an understandable discussion where the software developer is acting as a merchant, there seems to be little benefit to be gained in terms of player protection as the software/games are already subjected to external testing. There is also no reasonable case to be made to tax gaming software companies any differently to other software providers.

During discussions on the issue, the reasons for considering licensing were questioned:

- If the aim is to raise tax from the software companies it will be unsuccessful as they are likely to relocate so there will be nothing to tax;
- If the aim is to monitor the standards of software, a more effective method is to rely on overseas regulators ensuring software used by merchants licensed by them is acceptable;
- Licensing would not make it any easier to enter those markets where the Isle of Man is still on a blacklist eg Italy and Spain;
- It may be seen as discriminatory, and thereby create the impression that the IOM is not a good place to locate an online gaming business, or indeed any business.

PLACE OF CONSUMPTION TAX (POC)

POC is perceived by most to be unlikely to greatly impact the Isle of Man, but it is considered that it could have a significant effect on Gibraltar, where a much greater proportion of business is dependent upon UK clients. Nevertheless, the uncertainty, time and costs expended and reduction in net post-tax revenue when the 15% tax is imposed are certainly not helpful. A few people in the sector expressed some concerns that the introduction of the POC tax may provoke some operators to review their location and head for pastures new although what benefit they might gain from that would be unclear. The Department Of Economic Development, however, performed an impact analysis involving the key operators on the island and received confirmation that none were planning to review their location. On the contrary discussions have been held with some operators in other jurisdictions who may be considering moving to the Isle of Man.

ISLE OF MAN ADVANTAGES

There are many positive factors associated with being located in the Isle of Man but, with the notable and important exception of the absence of wealth tax and zero company tax, no unique selling point. However, as an overall package the Isle of Man can present an extremely positive message compared with other jurisdictions. This emphasis on the excellent all-round package

reflects comments of previous surveys but is even more relevant today as many of the perceived financial advantages are examined and eroded by external forces. Respondents to our survey were hearteningly enthusiastic about the Island, among the advantages reported (not in priority order) were:

- 30 years of continuous economic growth
- Close position to UK
- Taxation
- Increased understanding that we are a Business Centre rather than just a Tax Shelter
- Access to free market
- High quality infrastructure - big data requires high resilience and security and the Island's infrastructure has been set up to manage e-gaming data
- Competitively priced IT and communications compared with other offshore jurisdictions
- Access to Government is excellent and the good partnership between public and private sectors is appreciated
- Good legal system and absence of corruption
- High level of personal security with low levels of crime
- Staff - whilst it can be a challenge to find good staff once found they are very loyal
- Excellent quality of life
- Sense of community

In addition there are no fears of banking collapse or power cuts, no cross border issues and no concerns regarding place of establishment.

In summary, while there are no outstanding USPs associated with the Isle of Man, the existing cluster of industry-leading companies headquartered on the Isle of Man reported that with good infrastructure, support services and Government backing, combined with an absence of negatives and excellent quality of life means that the Island is very highly regarded by those who live and have business interests here. Furthermore, the forthcoming changes to VAT and gaming and other services transmitted electronically will boost opportunities on the Isle of Man as VAT will from 2015 be based on the Place of Consumption rather than the origin of the services.

IOM DISADVANTAGES

Many of the disadvantages of living and conducting business on the Isle of Man are unavoidable consequences of insular life while others are caused by external factors that cannot be controlled by a small jurisdiction, which must inevitably adapt to the global commercial and regulatory environment while having few opportunities to influence it. Survey respondents were on balance very positive but when pressed mentioned the following:

- Uncertainty of flight services. Air links to key UK airports are seen to be critical both to the quality of life and ability to conduct business effectively from the Isle of Man. Removal of these services is seen as a major threat to the Island and there was surprise that Government did not appear to have adequate policies to ensure the future sustainability of reliable, scheduled services to key destinations.
- VAT continues to be viewed as a disadvantage but one which those located here are able to balance against the otherwise good package of attractions. The changing circumstances surrounding VAT is producing unwelcome uncertainty and additional compliance costs of providing data for the calculation of the new sharing basis. However, 2015 VAT directive coming into effect in EU, said to be a threat to the online industry generally and not just the Isle of Man, may work in the Island's favour.
- Isle of Man, although unwarranted, is still on blacklists of some countries such as Italy and Spain.
- Some Government committees comprise too many members, this is said to impede their ability to provide quality and timely feedback.
- Health Services not as good as elsewhere, although it was recognised that there are inevitable difficulties providing an up-to-date comprehensive medical service with a small population base. However, whilst medical treatment differs between staff there are many first-class doctors and nurses. The administration and organisation appears to be capable of significant improvements.
- Concerns regarding the state of public finances and the capability of IOM Government to cope with reducing levels of VAT, particularly in the light of the high levels of Government employees with pension and other commitments
- Some suggestions have been made that we could increase the number of start-ups on the Island by decreasing the licence fees. Most observers however have concluded that this would lower the bar for the quality of company that we attract and would reduce substantially the fees that are collected from the sector. There is no evidence that we are losing out to other offshore jurisdictions on quality business due to the size of the licence fee.

- Comment and concern was made following the Isle of Man budget about the impact of the changes to conditions applied to those opting for the annual tax cap of £120,000. Requiring a five year commitment is of concern to those who do not wish to risk £600,000 tax payment if there are any uncertainties attached to their future income. Commentators recognised that Treasury introduced the five-year rule as an anti-avoidance measure but argued that other anti-avoidance measures, lacking the disadvantage of the budget change, could have been used.

OTHER RELEVANT ISSUES

WORK PERMIT REGULATIONS

Although companies reported that their experience had been extremely positive, problems that had occurred have been where:

- a. someone already in a company transfers to a new role, it is suggested that there should be an automatic transfer of the work permit to cover the new job description
- b. where an employee within the worldwide organisation of a company is transferred to the Isle of Man there should be an automatic grant of work permit as under no circumstance would that job be given to an outside party and there is a risk that the opportunity may locate elsewhere

Unique skills often need to be imported, these benefit not only the company but also the Island, as skills are passed on to the indigenous work force.

EDUCATION & TRAINING

ISLE OF MAN E-GAMING QUALIFICATION

The e-gaming industry typically is able and willing to provide good terms and conditions to attract high quality staff who are specialists in their area rather than generalists. In addition, specific relevant experience, qualifications and understanding, rather than a broad qualification, are considered to be far better than a general qualification covering all aspects superficially.

Concerns expressed:

- A general degree from an institution without a good international reputation would have only limited value
- Quality of lecturers – lecturers must be leading players and well known/respected practitioners from the Industry
- Qualification may be of limited value as the environment changes so quickly

- Distance learning offers opportunities for high-level tuition tailored to an individual so the future nature of education provision should be factored into any decision-making

Preference for some form of diploma was expressed, which would be useful in helping those wishing to transfer from other sectors and be an add-on to existing qualifications.

FUTURE

There is recognition that the industry has clearly matured and while there are new opportunities, such as crypto currencies, binary and FX business, there is an increasing tendency for clients to favour well-established, large companies. In order to cope with increased business and regulatory demands and so that companies can consider entering new markets, it has become necessary to have a sizeable team of legal, marketing and accounting professionals. These and other factors have raised the barriers to entry and are giving further stimuli to merger and acquisition activity.

The infrastructure laid down by the industry is enabling other aspects of e-business to be developed on the Isle of Man. Ancillary services such as software providers and hosting centres recognise the opportunities to diversify into activities such as BioMed. The increasing diversification of the mature, financially robust e-gaming sector into wider e-business activities makes it increasingly difficult to distinguish between online gambling and other e-business. Now that e-gaming has performed the task of stimulating the infrastructure and providing the skills, while continuing to recognise the importance and support the needs of e-gaming, it may be time to consider how best to focus on developing diversification opportunities while continuing to ensure the business climate continues to be attractive and updated to meet the needs of core e-gaming activities.

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