

The Cairn Gorm funicular and HIE's court cases - recovering public funds?

Description

The accounts for Natural Assets Investment Ltd (NAIL) ([see here](#)), the zombie company which bought Cairngorm Mountain Ltd (CML) from Highlands and Islands Enterprise (HIE), were published at the end of September. NAIL placed CML into administration after the funicular became unsafe to operate in 2018 and was one of the parties HIE subsequently sued. In August HIE announced they had recovered £11m from the parties involved but did not provide further details ([see here](#)) NAIL's accounts help to reveal a little more:

25. POST BALANCE SHEET EVENTS

On 13 July 2022 Natural Assets Investments Limited c
Enterprise (HIE) and certain other parties for the settlement
relating to the insolvency of Cairngorm Mountain Lim
to the insolvency of CML. No findings of fault were
claims primarily related to guaranteed dilapidations o
exceptional expenses of NAIL is £1m which the directo

Extract from accounts from 1st Jan - 31st Dec 2022 published on 29th September 2023. The same

First, a clarification. It appears the 2022 date, over a year before HIE made its announcement, may be a typo which should have read 13th July 2023. That is also suggested by the heading, "post-balance sheet events", and it would help explain the provisional allocation of £1m which the directors consider to be its appropriate share of the total settlement cost. It would also fit with the information provided by the Scottish Courts Service ([see here](#)) that three live actions concerning the funicular were extant this time last year.

The note is important, however, as it reveals that there were two different elements to the case HIE took against NAIL and its main shareholder. The first related to financial guarantees that had been provided when HIE sold CML to NAIL for £200k, the second to dilapidations. The note implies that most of the £1m NAIL agreed to pay HIE was for dilapidations and was agreed with "No findings of fault".

What the note does not say is how much the main shareholder and multi-millionaire, David Michael Gorton, had paid under the personal guarantees he had provided HIE, i.e his share of the settlement agreement. We still don't know therefore how much of the £11m HIE recovered in the court cases was from NAIL/Gorton and how much from the designers and builders of the funicular, let alone how

much if anything was paid in court costs (the “No findings of fault” suggests each side will have paid their own costs).

The financial guarantees provided by NAIL and Gorton

NAIL is apparently a financial basket case, a zombie company whose income after operating costs was insufficient to meet the interest on its debt payments right from the start. Since it was incorporated in February 2011, its net liabilities have increased by about £5-6m year on year. 2022 was no exception and its net liabilities increased to over £61m:

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NATURAL ASSETS INVESTMENTS LIMITED

CONSOLIDATED STATEMENT OF FINANCIAL POSITION 31 DECEMBER 2023

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NET CURRENT LIABILITIES	
TOTAL ASSETS LESS CURRENT LIABILITIES	
CREDITORS	
Amounts falling due after more than one year	
NET LIABILITIES	

With "current assets" of £568,119 at year end NAIL did not have the money to pay HIE £1m and with the Income statement showing revenue of only £1,596,968 that is unlikely to have changed this year. One way NAIL could pay the £1m it has agreed with HIE is to sell off some of its remaining assets.

One of the "investment properties" shown on the balance sheet is at John O' Groats where in 2011 HIE agreed to pay one of NAIL's subsidiaries, JOG Highland LLP, a third of the cost of a new tourist development there.

9 Accruals and deferred income

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Balance at 1 April 2014 & at 31 March 2015

During the year ended 31 March 2013 the LLP signed an agreement with Highlands and Islands Enterprise of up to £1,807,500 or 30% of the cost of O'Groats, Scotland. The grant is repayable up until 10 years after the grant and is therefore included as a liability until that point in time.

That grant, which was paid over three years, was repayable if the property was sold within ten. That condition still applied and was shown in NAIL's 2022 accounts, albeit with a slightly reduced amount of £1,446,000.

18. CREDITORS: AMOUNTS FALLING DUE AFTER M YEAR

Bank loans (see note 19)

Other loans (see note 19)

Deferred government grants

Government grants relate to a development grant received from
John O'Groats, Scotland. The grant is repayable if any prop

That condition comes to an end in this financial year, 2023-24. It means NAIL could sell the development at John O Groats and use the proceeds from HIE's £1,807,499 interest free grant to pay them back £1m. Does that sound like a good deal for the public?

Until then NAIL could have decided to sell off one of its other assets or get another loan from its main shareholder, David Michael Gorton. Why, might you ask, would he do this for a zombie company? The most likely explanation, I would suggest, is that NAIL and its subsidiaries companies have been used by Mr Gorton, quite legally, to reduce tax liabilities and avoid paying tax.

Mr Gorton is so rich (he is another who appears to have made £millions during Covid) that owning a company with net liabilities of over £60m actually becomes an advantage. However much HIE has managed to extract from Mr Gorton as a personal guarantee it should be seen in that context: his fingers have been ever so slightly warmed, not burnt.

The failure of our public authorities to recognise NAIL for what it was and is

How NAIL operates may be quite lawful but our public authorities in Scotland should not be having anything to do with their like. So far the Scottish establishment has shown little interest in asking how such an unproven company and its operating side-arm, Natural Retreats, was handed so much business by public authorities in a short time period: not just Cairn Gorm and John O Groats, but Lews

Castle (another procurement scandal) and Scottish Canals (who handed over their lettings business to Natural Retreats and then had to pick up the pieces).

In the case of Cairn Gorm and in the light of NAIL's settlement, it is worth re-visiting Audit Scotland's whitewash report of 2020 ([see here](#)) on HIE's management of the mountain businesses and funicular. The report found that while HIE had ignored the procurement rules about financial thresholds in NAIL's case but this was acceptable because of the guarantees they had sought:

17. NAIL did not meet the minimum financial standing threshold because of concerns over levels of debt and operating losses at the company and its subsidiaries. But under the qualitative moderation part of the test, NAIL submitted additional information that emphasised that the debt was mostly owed to its majority shareholder and should effectively be treated as equity. It claimed that the operating losses were due to the company being in an acquisitional phase as it looked to develop and grow. This additional information allowed NAIL to pass the minimum threshold and achieve an overall score that meant it could progress to the competitive dialogue stage. HIE obtained professional advice and concluded that the approach taken was appropriate.

It was evident well before Audit Scotland published their report, with liabilities increasing far more quickly than assets, that this was poppycock. Moreover, shares are not the same as debt, with dividends and interest payments governed by different rules and having different consequences (including for tax). HIE's comment about NAIL being in "an acquisitional stage" is particularly interesting given the connections between HIE and NAIL elsewhere in the Highlands and the public subsidies being used to support NAIL's growth. HIE clearly thought this zombie company was going to go places!

None of this mattered, however, because HIE took steps to mitigate its exposure to the risks:

HIE identified risks in relation to NAIL's financial situation and took steps to mitigate these before awarding the contract

20. The additional information provided as part of the qualitative moderation exercise made it clear to HIE that NAIL was dependent on loan support from its majority shareholder. HIE recognised this as a risk in its assessment of NAIL's financial standing, as reliance on one individual leaves a company vulnerable to changes in the circumstances of that individual, or that individual deciding to withdraw support.

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Part 1. HIE's decision to tra

21. To mitigate this risk, HIE negotiated a parent company guarantee with NAIL and a personal guarantee with its majority shareholder. HIE expected that these guarantees would allow it to recover funds from NAIL or its majority shareholder if CML did not meet its contractual obligations. HIE satisfied itself that funds were available to support the guarantees. This demonstrates that HIE understood the risk that came with awarding the contract to NAIL and acted to protect itself from that risk.

How well HIE protected itself remains to be seen. We won't know that until the total amount paid by NAIL and Gorton is revealed and how this compares to all the costs involved in first outsourcing CML and then taking it back into public ownership.

However, the much more important question which the Audit Scotland report failed to consider is whether the Public Sector's flirtation with big finance and its zombie companies is in the public interest. Scotland has come to quite a place politically when everyone can see something is wrong except for the governing class who hide behind governance (the professional advice sought by HIE to cover their backs) and guarantees.

Dilapidations

Re-reading the Audit Scotland report, it is more useful for understanding the money HIE may recovered for dilapidations and what this covered. Cairn Gorm was in a very dilapidated state at the point of sale and as a result HIE committed to investing £1.7 million in the resort as part of the deal to transfer CML to NAIL.

Exhibit 3

HIE's expenditure on Cairngorm Mountain, 2014-18

HIE spent over £3.5 million on Cairngorm Mountain between June 2014 and December 2018.

Project	Investment (£)
Dilapidation works and ski tows	1,725,236
Snow-making equipment	985,115
General repairs/ engineering works	576,945
Review of uplift infrastructure	148,496
Grants to CML	105,617
Miscellaneous spending	11,490
Total spending	3,552,899

Source: HIE analysis of spend

The £1.725,000 is the sum referred to above. The snow making equipment was purchased AFTER the funicular broke down

This suggests HIE invested c£600k on top of the dilapidation work and snow making equipment (and presumably covers additions like the new Shieling Rope tow ([see here](#))).

What NAIL/CML were required to invest under the terms of the sale of the company was set out in the lease for the ground and infrastructure. The Audit Scotland report, however, revealed that the lease was unclear and that what counted as maintenance was then disputed, e.g:

43. Despite this, disagreement continued. In 2017, HIE informed CML that although snow fencing could be included in maintenance costs, vehicle maintenance and road clearing should not. It told CML that it had been a mistake to concede in 2015 that those costs could be included. **Exhibit 4** shows HIE's assessment of CML's annual maintenance expenditure from 2014 to 2018 and reflects HIE's view of what items could be classified under maintenance expenditure. Maintenance costs for vehicles, piste machines and salt are therefore not included. We did not seek to verify the amounts or classification. This is the subject of ongoing legal action.

By the time they went into administration CML under NAIL should have paid c£2,165,000 but according to HIE had paid:

Exhibit 4

HIE's assessment of CML's maintenance spend

HIE considers CML spent £1.88 million on maintenance between June 2014 and when it went into administration.

Period	Expenditure (£)
11 June 2014 to 31 March 2015	260,088
1 April 2015 to 31 December 2015	353,777
1 January 2016 to 31 December 2016	476,861
1 January 2017 to 31 December 2017	394,204
1 January 2018 to 29 November 2018	392,856
Total	1,877,786

Source: HIE Property Team records of maintenance expenditure

That is a shortfall of c£290k. In addition the Report showed that CML/NAIL had failed to pay the required amounts into the asset replacement fund.

37. As part of the lease agreement, CML was to make payments to an asset replacement fund and two sinking funds. The asset replacement fund was intended to pay the costs of relevant replacement and/or upgrade works. The two sinking funds were to pay for maintenance of fixtures and fittings, and to meet buildings maintenance obligations respectively. When CML went into administration in November 2018, it had paid £33,000 into the asset replacement fund comprising £11,000 fixed deposit and £22,000 of variable deposit. The total fixed deposit due by 31 March 2018 was £80,000. The first payments to the sinking funds were not due until 31 March 2019 and so there was no requirement for CML to have paid funds into them at the time it entered administration. In summer 2018, NAIL attempted to renegotiate the terms of the sinking funds, as delays to its planned capital investments meant that its projected income was likely to be lower. This was still being discussed with HIE when CML went into administration in November 2018.

The two

shortfalls come to around Â£360k and are likely to form part of the Â£1m sum that was recovered. The rest remains to be explained.

It is important here, however, not to lose sight of the wood for the trees. Ever since the construction of the funicular, the rest of Cairngorm Mountain was being gradually run down and that process continued under Natural Retreats (as documented by many posts on this blog). One of the questions HIE should be made to answer in front of the Public Audit Committee is whether the Â£500k annual investment required was enough and how much they have had it invest in fixing dilapidations compared to the cÂ£1m recovered from NAIL.

Category

1. Cairngorms

Tags

1. Cairn Gorm
2. funicular
3. HIE
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5. Scottish Government

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Author

nickkempe