

# A Celebration of Autonomy 1204–2004: 800 YEARS OF CHANNEL ISLANDS' LAW

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Normandy by King John and the granting of  
special constitutional rights and privileges to  
the people of the Channel Islands.*

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EU in extending rules and disciplines on business taxation to non-members without their consent is in breach of these principles.

As far as Protocol 3 is concerned, it may be that the radical alternatives of abolishing the Protocol or, on the other hand, seeking full EU membership, can be ruled out. On the other hand, Jersey will certainly wish to examine the situation of other comparable jurisdictions (as has been done in outline in this paper), especially as regards their legal relationship with the EU, in order to see whether alternatives to Protocol 3 exist which might better guarantee the Islands' twin aims of political stability and growing economic prosperity. It is clear that other jurisdictions (both sovereign and non-sovereign) affected by the recent negotiations on the "tax package" with the EU will also be reviewing their status and relationship to the EU, with a view to possible change.

#### CONCLUSION

In the course of the last 15 years (not to mention the 31 years since Protocol 3 entered into force) all the major elements involved in Jersey's relationship with the Union have changed fundamentally. These include change within Europe itself – from customs union to Single Market and economic and monetary union, from Community to Union and from a multiplicity of founding Treaties to a single Constitution. In the United Kingdom, constitutional change – marked by devolution – is still in progress. In Jersey itself economic and demographic changes have produced a situation in which the Island is no longer a tranquil haven sheltered from the winds of change emanating from international organisations such as the EU, OECD and the UN, or important states such as the United States. The success of the financial services industry has not only generated prosperity for Jersey, it has also made the Island a serious "player" in the international financial community. In one sense, it may be said that, although Jersey has become an important member of the international financial community, it is handicapped compared with many of its competitors, by its international status (or lack of it). Thus, Luxembourg, Cyprus and Malta as full members not only of the EU but also the OECD, have the full power to "opt out" or even to "veto" tax measures taken in those organisations. Jersey, on the other hand, despite carrying the full weight of responsibility – without external assistance – for its own economic prosperity, lacks the defences available under public international law to enable it to resist unwanted initiatives by more powerful neighbours.

Jersey has been the target of unsought and hostile action by the EU, by the OECD and even by individual States, such as the United States and a number

### *Jersey's Changing Constitutional Relationship with Europe*

of its constituent States. Jersey has found it politically impossible to avoid responding to these initiatives. It has in fact responded constructively. Lord Falconer's speech to the States of Jersey on 10 May 2004 bears eloquent testimony to Jersey's constructive cooperation, but fails to address the serious underlying constitutional issues involved.

In these matters, the limited material scope of Protocol 3 has afforded no legal protection for Jersey whatsoever. In one sense, the fact that Protocol 3 is so manifestly "out of kilter" with the modern Jersey economy may be a source of confusion or misunderstanding about Jersey's status and "economic personality". Perhaps even more significantly, the UK has exercised its responsibilities for Jersey's international relations not by defending the Island's laws and practices, but rather by joining with those seeking to compel change, notwithstanding the absence of internationally-binding rules or procedures.

These circumstances have forced Jersey (as well as other UK dependent territories) to come to terms with the relative weakness and vulnerability of its constitutional and international situation. By a mixture of political will and technical excellence and by making the most of its legal autonomy (mainly internal, but also to a limited degree external), Jersey has succeeded in

- (a) preserving its status as a cooperative jurisdiction in the OECD;
- (b) reaching an accommodation with both the UK and the EU as regards the "rollback" of its company tax legislation under the EU Code of Conduct;
- (c) reaching agreement with the EU and its Member States<sup>122</sup> on the implementation of a retention tax system for the implementation of the TOSD;
- (d) reaching agreement with the EU, through the UK, on the alignment of Protocol 3 with the EU Constitution.

In this process, Jersey has been forced to recognise the vulnerability of its international and constitutional position. Despite a recent strengthening of the action taken, inter-ministerially, in London by the Department of Constitutional Affairs (DCA) in defence of Jersey's interests, it may safely be said that, at least in relations within the EU and the OECD, defending the interests of the Crown Dependencies (especially when these conflict with those of the UK) is not a UK priority. This was certainly true in the recent tax negotiations in the EU and the OECD, but it is also the case (whether for

<sup>122</sup> Formally, of course, the TOSD Agreements are with the 25 Member States individually. The terms of the Agreements were however settled by direct discussions with the Commission and the Irish Presidency of the Council.

Jersey, Guernsey or the Isle of Man) on issues such as the application of the agricultural state aids or safeguards provisions of the Protocol. Recent experience in ensuring that Jersey does not suffer economic harm as a result of the adoption of the UK or EU Single Market measures (e.g. as regards payments systems for banks) offers some hope for optimism. But, in general terms, Jersey's experience of the last few years tends to emphasize the need for far greater international autonomy or "personality"<sup>123</sup> so that it can defend and enhance its hard-won political stability and economic prosperity, without having to go "cap in hand" to London and to rely – in effect – on one of the less-powerful departments of State to wring "concessions" from the Treasury, Inland Revenue, DEFRA or the Foreign Office.

It is no consolation to recognise that many of Jersey's competitors endowed with formal sovereignty (Liechtenstein, Andorra, Monaco and San Marino) have arguably fared not much better in the face of the political pressure brought to bear by the EU and its Member States (including the UK) and the OECD. Competitors such as Cyprus and Malta which have now joined the EU will now of course benefit from all the institutional rights accorded to Member States (e.g. the right to "veto" unwanted tax initiatives).

As far as Jersey is concerned, once it had been recognised that a compromise had to be made with the EU (for example on the TOSD), Jersey's performance in drafting a "Model Agreement" in concertation with Guernsey and the Isle of Man, in negotiating this with the Commission and Council Presidency, in finalising the agreements bilaterally with all 25 Member States and then ensuring domestic implementation, was unsurpassed, including by EU Member States.<sup>124</sup>

The clear lesson to draw from this experience is that Jersey has the political will, technical competence and resources to conduct international relations in areas where its interests are affected. It is not clear that the constitutional relationship with the UK significantly strengthens Jersey's international negotiating position. And in fields such as tax, where the UK has opposing interests, the UK link is entirely unhelpful. Precedents exist for UK dependent territories or colonies to act as international persons in their own right. Hong Kong was, for many years, a case in point, negotiating with the EC (including the UK) in fields such as textiles, where Hong Kong and UK and EU interests were diametrically opposed.

<sup>123</sup> In this context, it may be questioned whether the term "letter of entrustment" is appropriate in the modern age. Under public international law, it would suffice for the UK to make it known, both bilaterally and multilaterally that, whilst retaining its links with the Crown, Jersey enjoys international autonomy commensurate with its internal independence, for the sake of clarity and transparency, this transfer of external powers could well be set out in a statute.

<sup>124</sup> At the time of writing, a large number of the EU's Member States have failed to transpose the TOSD into national law, as required by the Directive, by the end of 2004.

### *Jersey's Changing Constitutional Relationship with Europe*

A word of caution is appropriate at this point. It is clear that even formal sovereignty would not be a panacea, a passport to instant international recognition and acceptance or even a means of avoiding challenges to Jersey's internal laws and practices. As indicated above, it is likely that as EU membership continues to grow and the *acquis* continues to expand and consolidate, the extent to which the EU will expect jurisdictions on its periphery and which wish to do business with the Union, to adopt the *acquis* (with or without relevant Treaty relations) will also increase. This will be so particularly in areas deemed by the EU to be politically sensitive and/or economically harmful, such as tax, financial services, economic crime and "internal affairs" (anti-terrorism, visa, asylum, immigration policy, etc.).

Jersey (and indeed the other Crown Dependencies) must prepare itself to meet these challenges. Like all independent and self-sustaining jurisdictions of its size, Jersey will have to make the best use of scarce resources. In my view, to focus exclusively on the existing legal link with the EC (although that has been the central theme of this paper) would be a mistake. The Protocol has, after all, only recently been reconsidered and renewed, virtually unchanged, in the IGC leading to the Constitutional Treaty.<sup>125</sup> This is not the case for the constitutional relationship with the UK, where the grant of external autonomy in areas falling within Jersey's internal competence, is now a matter of urgency. Priority does however need to be given to improving international knowledge and recognition of Jersey's political and legal status. Jersey's first-class track record of international cooperation also deserves to be better known. This is essential in order to provide greater legal certainty for Jersey's economic relations with its partners around the world, including perhaps first and foremost the EU and the United States.

Jersey's financial industries have been successful in publicising their products and services across the globe. Comparable efforts must be made by Jersey politicians and officials particularly in the EU, but also in the United States and other key jurisdictions.<sup>126</sup> It is disappointing that, despite a succession of informal but constructive meetings with EU (mainly Commission) officials in areas such as financial services, justice and home affairs and international economic crime, Jersey is too frequently identified as a "tax haven" or a jurisdiction which lacks – to a certain extent at least – full international legitimacy. There is a contradiction here which needs to be addressed perhaps by considering formalising or giving greater publicity to, meetings with the

<sup>125</sup> There is of course no reason why the longer-term future of the Protocol could not be considered immediately, since it would in any event take some years before the processes leading to its changes could be completed.

<sup>126</sup> This is the same challenge faced by literally hundreds of sub-State entities which have had to come to terms with the important role played by the EU in their political and economic lives. This explains why over 200 local authorities, regions and other entities have opened offices in Brussels.

EU institutions and the almost uniformly positive results emerging from these meetings. This is normal practice not only in the case of diplomatic contacts by States and international organisations, but even by private sector entities wishing to put on record (to avoid misunderstandings and for future reference) points made, understandings reached or even disagreements.

In my submission, now that negotiations have been successfully resolved both with the EU and the OECD on personal and business taxation, sustained efforts need to be made – at a level previously not attempted – to secure international recognition of Jersey's status as a self-governing jurisdiction with the highest regulatory and supervisory standards, not only in tax and financial services, but also in law enforcement and international cooperation more generally. Such recognition, once achieved, needs to be formalised in a way which can later be relied upon. Achieving a minimum degree of international legal personality, whilst retaining a clear link with the Crown, is a *sine qua non* in this respect. The problem until now in informal contacts with the EU has precisely been that the contacts were informal and therefore subject to no official records. Such recognition as has been received (for example as regards the excellence of Jersey's anti-money laundering legislation) is quickly dissipated, since it is not recorded<sup>127</sup> and quickly overtaken by other events in the minds of busy EU officials.

The label "tax haven" (or, even more vaguely, "off-shore" jurisdiction) and the consequent inclusion on national "black lists" or other forms of unwarranted discrimination, is more intractable. The very use of the term "off-shore" somehow connotes (or is seen increasingly, by the EU and US authorities to connote) a jurisdiction which escapes appropriate or normal regulatory and supervisory control and thereby creates unfair advantages for investors or traders, including non-residents.

The perjorative use of terms such as "tax haven" is particularly difficult to combat, given the technical complexity (and indeed lack) of agreed ground rules in, international tax law and policy. However, to the extent that such terms imply a failure to respect minimum standards in areas such as international economic crime and international cooperation in customs, tax and police matters, then the evidence and the means clearly exist to rebut such assertions.

As far as tax policy is concerned, it is clear that, both inside the EU and internationally, the limits of national fiscal sovereignty and the appropriate scope of international rules and disciplines have yet to be defined. EU and

<sup>127</sup> At least in the case of sovereign jurisdictions such as Andorra (or even, in the past, with non-sovereign jurisdictions such as Hong Kong and Macau) formal records are kept of regular Ministerial, diplomatic or official-level meetings. *Notes verbales* are exchanged, as well as agreements (even on minor matters) being recorded by exchanges of letters, memoranda or other instruments recognised by international law.

### *Jersey's Changing Constitutional Relationship with Europe*

OECD policy documents assert simultaneously that tax (rates and structures) is a legitimate instrument of national economic policy in promoting the competitiveness of economies and enterprises, whilst at the same time stating that "harmful tax competition" is to be condemned.<sup>128</sup>

As the current debate in the US election campaign demonstrates, the perceived loss of fiscal revenue (both at Federal and State level) is a crucial political issue in the United States, particularly in a nation with a massive budget deficit. The debate on tax rates and structures, as well as the extent to which international corporations should be permitted to structure or channel their operations (including invoicing and tax accounting) through multiple jurisdictions, including those classed as "off-shore", will continue for the foreseeable future. The absence of a truly global and inclusive forum for international tax discussions is a significant handicap to progress in this area.

In these circumstances, Jersey has a choice between continuing with its present level of international engagement, or of increasing it. Even small jurisdictions do not lack intellectual capital. Jersey has the opportunity to develop its international cooperation in international tax policy (and indeed in international economic relations generally), including the building of alliances with other jurisdictions which share Jersey's concerns. The EU institutions and the increasing number of Member States (many of which now may share Jersey's views of the use of tax policy as an instrument of international competitiveness) should not be excluded from a more pro-active approach in this field by Jersey and the other Crown Dependencies. Constructive engagement with the UK will inevitably be a vital element in any strategy which Jersey may adopt for its future international relations. In this respect, the Protocol which currently links Jersey to the EC (and in the future to the EU) is only one element in Jersey's increasingly complex and challenging international relations.

<sup>128</sup> In the EU, failing sufficient agreement between Member States on the elimination of "harmful" tax measures, the Commission has – since 2000 – adopted a more rigorous and extensive approach to its state aids policy, applying article 87(1) to national fiscal measures previously considered not to constitute "aid". At the same time, the Commission has failed to distinguish between tax measures affecting the competitive position of enterprises under article 87(1) and fiscal measures of a more general nature affecting competition between national economies, under articles 96–97 EC. EU fiscal state aids policy does not of course apply to the Crown Dependencies.

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