

**TAX INFORMATION EXCHANGE AGREEMENT WITH THE UNITED STATES OF AMERICA (P.172/2002) -
ADVICE OF H.M. ATTORNEY GENERAL**

**Presented to the States on 29th October 2002
by the Policy and Resources Committee**



STATES OF JERSEY

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The Policy and Resources Committee has decided to present to the States the advice given to the Assembly on 24th October 2002 by H.M. Attorney General so that the advice is available in the official records of the Assembly for future reference.

I am setting out below my advice to members of the Assembly on the proposed Tax Information Exchange Agreement with the United States of America which is the subject of P.172/2002.

At paragraph 9 on page 6 of the Report of the Policy and Resources Committee on the proposed Tax Information Exchange Agreement with the United States of America, it is said that "*the Attorney General has expressed his contentment with this approach and accordingly has confirmed to the Committee that the States has the necessary authority to proceed*". That statement was made in the context of the comments of the Committee on the letter of entrustment addressed to the Jersey Authorities enabling them to negotiate and conclude an Agreement with the United States, notwithstanding the United Kingdom's responsibility for the Island's international relations.

There have been some developments in the last two weeks, since that Report was lodged. I should say immediately that I do still recommend the Agreement to members, but there are some constitutional issues which I want to draw to their attention so that the decision which is made on Tuesday is an informed decision.

The document scheduled to the Report and Proposition is an Agreement concerning Information Exchange in Tax Matters. It is declared to be made by the Government of the United States and the Government of Jersey. Because of its subject matter (tax) it is sensitive. Jersey places some store by its autonomy in tax matters. The drafting of the Agreement was deliberately designed to express clearly that the obligations which were assumed by Jersey were indeed Jersey obligations and not those of the United Kingdom. In our negotiations with the United States officials, we made this point regularly and clearly. That is well documented.

My understanding is that the United States requires that the obligations under these types of Agreements be legally enforceable. It is this requirement for legally enforceable obligations which has caused us a difficulty because international law would normally only recognise the obligation as a legal obligation if it were in a Treaty or Convention made by a fully independent State. Jersey does not have that status in international law. It is a dependency of the British Crown, and of course there is internationally - and perhaps domestically - much confusion and some uncertainty as to what legal consequences flow from that status. This confusion might disappear if the Island were to develop a structured but possibly limited international personality, and obviously would disappear if it were to become an independent state.

The making of Treaties and Conventions falls within the Crown prerogative. In practice, the power to make them has in the United Kingdom devolved upon Ministers of the Crown who form Her Majesty's Government. If such Treaties are made which require changes in the domestic law of the United Kingdom, the Government presents such legislation to Parliament for consideration. Because there is a party system, the Government can be reasonably certain, in most cases, that Treaties which have been made by Ministers can in fact be implemented in domestic law.

Jersey's position in this international context is unusual. We are regularly consulted by Her Majesty's Government whenever Treaties or Conventions made by the U.K. come to be ratified in order that we may express a view as to whether that ratification should include the Island. Responsibility for reaching a conclusion on that consultation is exercised, as part of its responsibility for external relations, by the Policy and Resources Committee, which acts closely with the Law Officers, because it is important that if the international obligation is assumed by the United Kingdom on the Island's behalf with our consent, we have the domestic law or practical administrative arrangements in place to ensure that we will not unwittingly place the U.K. in breach of that obligation.

The structure of the OECD Harmful Tax Practices initiative which commenced in 1998 does not sit easily with this constitutional relationship between Jersey and the United Kingdom. In effect, the Island was left to deal directly with the OECD and to make its own commitments to the OECD in relation to the administration of its own tax affairs. That in itself amounted to a recognition that the Island has autonomy in domestic tax matters. Members will remember that the discussions were successfully concluded with a commitment made by the Island that it would exchange information in tax matters in accordance with Tax Information Exchange Agreements to be negotiated with individual countries.

Prior to making that commitment, the Island Authorities had written to the OECD to emphasize that Jersey did have fiscal autonomy which included the power to make its own arrangements as to exchange of information on such terms as it might negotiate.

The difficulties which arise on the one hand from one country - in this case the United States - requiring that the international obligation be legally enforceable, whilst on the other hand the Island considering that the subject matter of the obligation falls within our domestic autonomy, are considerable. As increasingly international Treaties and Conventions affect matters which are domestic to the citizens of the countries making those Treaties, the issue of the Island's international status comes to the front. This is not an issue which so far has troubled the States to any great degree, but it is probably as fundamental as anything members have had to consider recently. For reasons I will come on to shortly, I do not suggest that great consideration is given to these fundamental issues today. But I do suggest to members that there are some important underlying issues which need to be given mature, dispassionate and quiet deliberation over the forthcoming months.

Following some official correspondence in the early part of the year between Her Majesty's Government and the Island Authorities, I attended with the approval of the Policy and Resources Committee a meeting with U.K. officials, and indeed with the Attorney General of Guernsey. As a result of that meeting a solution emerged, as a result of which Her Majesty's Government, on behalf of the Crown, agreed by the letter of entrustment that the Island could negotiate and sign a Tax Information Exchange Agreement with the United States. This was an important step forward for us, and reflects to my mind a declaration of trust in the Island by Her Majesty's Government, and a recognition that our tax autonomy is important to us and that in an international matter of this nature, it is for the Island to determine what it is prepared to agree.

The wording of the letter of entrustment was not discussed with us. At one level, it left open the question as to whether or not the obligations contained in the Tax Information Exchange Agreement were obligations in law of the United Kingdom or of Jersey. At the time the Committee lodged its Report and Proposition, I advised the Committee that -

- The entrustment was expressed adequately if not as I would have liked.
- Both the U.K. and the U.S. had been informed by the Island negotiators in no uncertain terms that the obligations were for Jersey alone.
- The wording of the Agreement itself points in that direction. Indeed in that context I draw to your attention that nowhere in the Agreement is there any sign of anything that would be done by the United Kingdom in relation to the obligations which are imposed on Jersey.

The debate was postponed two weeks ago because after the lodging of the Report and Proposition, the United Kingdom sent to the Island Authorities a copy of a diplomatic note which had been sent to the United Kingdom by the Government of the United States and which referred to the United Kingdom's legal responsibility for the Island's external relations. The United Kingdom's note to the United States is in the same terms. The President of Policy and Resources agreed to my request for time to consider whether this had any impact on the advice which I had given to the Committee, and would give - and am now giving - to the States.

Is this important? The answer is that one cannot be entirely certain. There is a view - indeed it was the conclusion of the Report of the Royal Commission on the Constitution in 1973 (the Kilbrandon Report) that if the United Kingdom has an international obligation, then it must have the legal power to take such action as is necessary to ensure that the United Kingdom does not breach that obligation. Taken to its logical conclusion, that might mean that if there were an international obligation binding on the United Kingdom as a result of this Agreement, the United Kingdom might assert that it was in law entitled to take action to ensure that Jersey performed its obligations. Quite what that action might be is entirely hypothetical, and it would I think be fruitless to indulge in conjecture.

There is an alternative view on this question as to whether or not it is important that the creation of a legal obligation on the part of the United Kingdom confers legal power on the U.K. to take action in respect of our domestic affairs. I referred to this in the statement I made to the Assembly on 14th May 2002. I think the alternative view is the better one, but only a court of law could resolve the divergence of view, and fortunately our relations with the United Kingdom make such a course of action a very unlikely last resort. The alternative view I remind members is that the exercise of a Royal Prerogative to make Treaties has no impact in domestic law unless and until the democratically elected legislature so resolves. If that is so, then unless Parliament has a power to legislate for the Island - which you will recall was a question I answered in the negative in the same statement some months ago - it would lie only with the States to determine what changes in legislation or in administrative practice were appropriate in relation to the Tax Information Exchange Agreement.

It is of course a corollary of the alternative view which I have expressed that the making of a Treaty on behalf of the Island places the United Kingdom in the unenviable position of having an international obligation without the legal power to ensure that that obligation is met. That of itself is a reason, so it seems to me, why in all these international matters, the Island must act with the greatest of care and responsibility.

Following the receipt of the exchange of diplomatic notes which I have mentioned, some official communications took place with Her Majesty's Government (H.M.G.). In particular, having regard to Article 13 of the Tax Information Exchange Agreement, the Island Authorities asked H.M.G. to confirm that the termination provisions could be exercised by Jersey without let or hindrance by the United Kingdom. This question was addressed on the assumption that a court decided, in the unlikely event that it ever was called on to decide, that the obligations under the agreement were U.K. obligations. The Island Authorities also asked H.M.G. to confirm that the United Kingdom would not interfere directly or indirectly with the performance of the Island's obligations under the Agreement, and during its continuance.

Responses have been received that while the United Kingdom would wish Jersey to consult the United Kingdom about termination, the U.K. would be unlikely to stand in Jersey's way. On the second point, the response was that the question was hypothetical, and that the U.K. has no desire to interfere with the Island's performance of any obligations which it has entered into under the Tax Information Exchange Agreement.

As a matter of constitutional law, I advise members as follows -

1. There are arguments both ways as to whether or not the obligations contained in this Tax Information Exchange Agreement on Jersey's part to be performed are in international law the obligations of the United Kingdom or of Jersey.
2. If the obligations are obligations of the United Kingdom, there are arguments in constitutional law both ways as to whether or not the United Kingdom has any legal power to enforce performance of those obligations.
3. The process which has been adopted in the instant negotiations, both with the U.K. and the U.S. has revealed some significant constitutional change in that for the first time, albeit limited to this Agreement only, the United Kingdom has agreed that the Government of Jersey can negotiate and conclude an International Agreement as a result of which the Island will undertake the performance of certain international obligations.

I draw to the attention of members that in order to perform this International Agreement it is essential that changes be made to the Island's Income Tax legislation to confer power upon the Comptroller of Income Tax to obtain and exchange the information which is proposed to be exchanged pursuant to this Agreement. Members must be under no doubt about that, even though the legislation has not yet been drafted. When that legislation comes to be presented to this House, there may indeed be debate about the detail of it but the principles underlying it which I have mentioned will I hope cause no difficulty. Making the decision to authorise signature of this Agreement does involve agreement in principle to changes in the Island's tax legislation.

I hope members will not have found this exposé to be too drawn out. The underlying issues are in fact extremely important and will crop up again and as these debates do not often surface in the States Assembly, it was I thought useful to give voice to them and the advice at this time.

Having given the legal advice, I hope I will be forgiven for drawing to members' attention some practical points. On the one hand the issue arises as to whether by making this Agreement with the U.S. the Island will have conceded the principle of creating an U.K. obligation, if it does, in respect of our domestic tax matters. This is potentially difficult but I think it should be possible to clarify our position on any subsequent occasion. Indeed, it may well be that different considerations will arise in relation to future Tax Information Exchange Agreements to be negotiated with other countries, particularly perhaps with E.U. member states, and these should be fully examined on a case by case basis as the need arises in the future.

On the other hand there are these points which in my view would militate in favour of a decision by the Assembly to endorse the making of the Agreement. These are -

- It appears to me that it is highly unlikely there will ever be any constitutional argument over the performance of these obligations. The United States and the Island will have made the Agreement in good faith and there is every reason to suppose that we will perform our obligations which arise out of it. To the extent that we reach a different view from the United States on any particular request, there is provision in the Agreement for the competent authorities to use their best efforts to resolve the matter by mutual agreement. Ultimately the power to decline a request remains with the United States and with the Island, in accordance with Article 7.
- Completion of this Tax Information Exchange Agreement will be an important signal internationally that the Island gave its commitment to the OECD in good faith. That is important. The converse is that if the international community should believe that our commitment meant nothing, we could no doubt expect to see a revival of the OECD threat of being listed as an uncooperative jurisdiction.

- The Agreement itself has been negotiated with the United States having regard to the Model OECD Tax Information Exchange Agreement, and to other Agreements which have been made internationally with the U.S. The Island is not in fact undertaking any more onerous obligation than many other territories and countries have undertaken.
- The Internal Revenue Service of the United States has already accepted the Island as meeting the criteria for recognition as a Qualified Intermediary which thus indicates a relationship with the U.S. which is not necessarily replicated with other countries.

It is of course entirely a matter for members, but the balance of these points is such that I commend the proposition to make the Agreement to members as a pragmatic course which we should adopt and as an appropriate signal of our international responsibility.

H.M. Attorney General

22nd October 2002