

**STATEMENT TO BE MADE BY SENATOR FRANK HARRISON WALKER, PRESIDENT OF
THE POLICY AND RESOURCES COMMITTEE, ON TUESDAY 10th JUNE 2003**

I should like to make a statement about the outcome of last Tuesday's meeting of EU Finance Ministers (ECOFIN) and its implications for Jersey.

After some six years of negotiations, ECOFIN finally agreed what is known as the EU Tax Package. Two parts of this package have implications for Jersey. First, the EU adopted a Directive for the Taxation of Savings Interest. And second, as a result of its work on a Code of Conduct for Business Taxation, the EU reached agreement on a timetable for standstill and roll-back of 66 so-called harmful tax measures, of which four related to Jersey.

For reasons I will explain, I believe the outcome, taken as a whole, is a very satisfactory one for the Island. We are, of course, not part of the EU and therefore not subject to EU fiscal legislation and we are determined to defend our longstanding fiscal autonomy and our best economic interests. Nonetheless, conditional on the approval of the States, we consider it is in the Island's best interests to adopt a good neighbour policy and agree to make changes to our own tax system that reflect aspects of the EU Tax Package. Before coming to the details of what we intend to propose to the States, I would like to remind you of our strategic approach, and of our successful negotiations on behalf of the Island.

Our consistent aim has been to sustain and promote Jersey as a pre-eminent international financial jurisdiction. We believe that a high international standing for Jersey brings tangible rewards to our finance industry and to the Island generally. This good reputation is best achieved by constructive engagement with international institutions and governments. This policy was actively promoted by former Senator Pierre Horsfall, my predecessor as President of the Policy and Resources Committee, to whom I gave my full support. I am sure you will wish to join me in paying tribute to Pierre Horsfall for all his hard work and for what he achieved on this front.

There are a number of steps we have taken in recent years to demonstrate our policy of constructive engagement.

- (i) First, we have participated actively in the international fight against money-laundering and terrorist financing and Jersey's efforts in this area have been widely recognised internationally by such organisations as the IMF, the FATF and the Financial Stability Forum;
- (ii) Second, we announced last year that we were prepared to enter into a general political commitment to exchange tax information, in response to specific and justifiable requests, with OECD countries; and,
- (iii) Third, we have demonstrated our intention to implement our commitment to the OECD with the signing of a bilateral Tax Information Exchange Agreement with the United States of America.

The main aims of the EU tax initiative have been to defend the tax revenues of the member states, to eliminate harmful tax competition within the EU, and to support the aim of creating a genuine EU single market. Because the member states of the EU cannot control the movement of capital across borders, they have been keen that certain third countries, together with the associated and dependent territories of member states, should introduce the same or equivalent measures to prevent circumvention of their own internal proposals. Since 1997, this has been an explicit condition on the part of the member states for agreement to the Tax Package, and Jersey was one of the jurisdictions from whom the EU sought cooperation.

In keeping with our overall strategy of constructive engagement, we have sought to help the EU achieve its objectives. But we have always stated very firmly that, in doing so, we were determined to defend the Island's best interests. We also have made clear that any agreement we entered into would be conditional upon the existence of a level playing-field, and would be subject to agreement by the States.

The changes sought by the EU were of two kinds. First, they wished to see the roll back of so-called harmful tax measures which discriminated between resident and non-resident taxpayers, which in Jersey applies

particularly to exempt companies and international business companies. This is the Code of Conduct agenda. Second, in the shape of the Directive on Taxation of Savings, they wished to ensure payment of appropriate taxes by individuals resident in the EU, and I would repeat individual EU residents, in receipt of interest in their own name from Jersey financial institutions. I am stressing that this applies to EU individual residents because in the context of the Directive nothing in the proposals, nor in our response, will affect people who are not residents of the EU. The proposals equally do not affect companies nor almost all forms of trusts.

For Jersey, Code of Conduct measures were by far the more important. Tax neutrality is the bedrock on which our financial services industry is built. Furthermore, the changes initially sought by the EU if adopted would have had a significant impact on the business we attract on a world-wide basis and not just from within the EU. So we made it clear to the EU that we would only be prepared to phase out the measures deemed harmful by the Code of Conduct Group if we could do so in a way that allowed us to preserve our tax neutrality and competitive position. We also made it clear that any changes in our fiscal arrangements would need far more time to implement than was foreseen in the Code of Conduct Group's own timetable. Only if our conditions were satisfied were we prepared to discuss co-operation on the linked issue of the Savings Tax Directive.

I am pleased to say that our approach has been successful. The EU are content with our proposal for an extended timetable for phasing out the so called harmful tax measures. They have also accepted our proposal to replace exempt companies and international business companies by a general zero rate of corporate tax with an additional but competitive rate for financial services businesses. This will preserve Jersey's tax neutrality and competitive position for financial transactions. The ECOFIN decisions give an international seal of approval to these arrangements. This is indeed a very satisfactory outcome for Jersey.

In return, we are prepared to honour our commitment to act in support of the EU on the Savings Tax Directive. Most EU Member States, including the UK, have favoured achieving the aim of the Directive through automatic exchange of information between tax authorities. Under this, home tax authorities would be told automatically about interest payments to their residents received from another member state. We have long made it clear that, subject to a level playing-field, Jersey would also favour automatic exchange of information as the way forward. This was also the majority view of the finance industry and is consistent with Jersey's positioning as a high-quality international financial jurisdiction. Jersey does not want to be seen as a haven for those with something to hide.

Regrettably, the EU has not ensured the level playing-field that we sought. On 21st January 2003, ECOFIN signed up to two alternative outcomes on the Savings Tax Directive. Twelve Member States opted for automatic exchange of information. But the remaining three, namely Austria, Belgium and Luxembourg, were allowed instead to introduce a withholding tax as an alternative to automatic exchange of information for a transitional period. This will end when Switzerland and the other specified third countries provide for exchange of information on request in accordance with the OECD tax initiative. The EU plan is that the withholding tax will start at 15% in 2005, rising over time to 20% and then to 35% by 2011. This withholding tax option is also favoured by the specified European third countries, of which the key one from our perspective is Switzerland. As one of our major competitors we are keeping a very watchful eye on all developments between Switzerland and the EU.

There is no guarantee that the three EU Member States or Switzerland will move to an automatic exchange of information regime in 2011 or even thereafter. Furthermore, the creation of a minimum 6 year transitional period with withholding tax rates at relatively minimal levels could potentially give those countries a significant competitive advantage. The result of this is not the planned common standard for all based on automatic exchange of information but rather a dual system approach which yields a playing-field on two very different levels.

Guernsey came to this conclusion in early April and declared its intention to adopt the withholding tax option. We deliberately delayed any announcement of our decision in this respect until we knew for certain that the position on the Code of Conduct was secure and we had had further consultation with the finance industry both through a formal survey and informally. We have also held discussions with Guernsey and the Isle of Man. In addition we have also reviewed our competitive position more generally conscious of the fact

that there are competitor jurisdictions such as Singapore and Hong Kong whose co-operation has not as yet been sought by the EU .

In the light of this we have thought it wise to reconsider our initial position in favour of automatic exchange of information. This has not been a straightforward decision, because there are valid arguments in support of both options. But a majority of our industry has told us that, in the absence of a level playing-field, they would prefer us to adopt the withholding tax option rather than automatic exchange of information. This squares with our own analysis: we believe we would be less competitive if we introduced automatic exchange of information while other key competitor jurisdictions had only a low-level withholding tax, particularly during a rather lengthy transition period of 6 years. This is reinforced by the decision of Guernsey and now the Isle of Man to go the withholding tax route.

Policy and Resources therefore intend to recommend to the States that Jersey should adopt, in the short term, the withholding tax model on the same timetable and at the same rates as the three EU Member States and named third countries, including Switzerland. It is important to understand, however, that in taking this route information exchange will remain an option for individual EU residents should they wish to take advantage of it. Individuals who would prefer to have their interest income disclosed to their home tax authorities instead of paying the withholding tax will have the option to elect voluntarily to have such information exchanged. This confers, as a consequence, greater flexibility for those affected.

Although the UK government has vigorously promoted automatic exchange of information they were party to the ECOFIN decisions and understand our reasons for favouring the withholding tax option.

We will remain consistent and constructive in our approach. We remain committed to automatic exchange of information subject to the condition of a genuine level playing-field. In the absence of an EU agreement that fulfils this condition the Policy and Resources Committee believe that the Island has been left with no alternative, in protecting its economic interests, but to adopt the withholding tax option in common with its main competitors. Given the current options, we believe we have chosen the best course of action for Jersey. Above all, with the satisfactory outcome on the Code of Conduct, we believe Jersey can again look to the future with a renewed sense of certainty and confidence.

The Policy and Resources Committee will be bringing specific proposals to the States in due course. The implementation of our commitments will only be undertaken on the same timetable as EU Member States and the other third countries. It will also depend on the negotiation of Tax Information Exchange Agreements with individual EU Member States including the UK. In negotiating those agreements we will be looking for evidence that our cooperation will be reflected in a more positive attitude towards business relationships with the Island than has often been the case in the past. There is much still to be discussed in consultation with the finance industry on the implementation of what we will propose to the States and we intend to prepare an interpretative note to assist the industry in planning for what presently is due to come into effect from 1st January 2005. We will keep the States informed on these and related matters.