



**KEYNOTE ADDRESS OF SIR PHILIP BAILHACHE,
BAILIFF OF JERSEY, AT THE LIECHTENSTEIN DIALOGUE ON THE FUTURE OF
FINANCIAL MARKETS**

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[Your Royal Highness], Your Excellencies, Ladies and Gentlemen,

It is a great privilege to have been asked to address this Dialogue on the future of financial markets. I am not sure why this privilege has fallen upon me and perhaps when I have explained the functions of the Bailiff of Jersey you may share that uncertainty. But I shall do my best nonetheless to justify my presence here and the generous hospitality shown to my colleague and me by the Liechtenstein government.

I should like to say just a few introductory words about the constitutional position of Jersey in order to set in context my remarks about the present and the future. Jersey is in constitutional terms a Crown dependency; it is not a colony nor is it an overseas territory of the United Kingdom. The relationship is with the Sovereign and dates back to 1066 when William, Duke of Normandy, invaded England and seized the English Crown. Jersey was then part of Normandy and our loyalty to the Duke became loyalty to the King of England. The loyal toast in Jersey remains a toast to La Reine, notre Duc, the Queen, our Duke. In 1204 King John of England lost continental Normandy to the French King and, in order to retain the loyalty of the strategically situated Channel Islands, conferred a number of liberties and privileges, including the privilege of self-government. Jersey's domestic autonomy dates from 1204.

This is not an address however on the constitutional position of Jersey and I will say no more about it, but I wanted to underline the long-standing autonomy of the Bailiwick, which is one of the critical framework conditions underpinning its position as a financial centre. Jersey enjoys, as an ancient constitutional privilege, the right to govern its internal affairs, including its fiscal affairs, while the United Kingdom is responsible for defence and external relations. Experience in the last eight years or so has taught us that it is sometimes necessary to defend our own international interests, and that we cannot reasonably or fairly expect the UK government to protect them on every occasion. We do not yet have the



sovereign status of Liechtenstein or Andorra, but we nevertheless seek a much greater responsibility for our external relations. But that too is another story.

And what is the Bailiff? Jersey is a Bailiwick, and the Bailiff is the civic head of the Island. He is not the Head of State, but he is appointed by and holds office under the Queen. The Bailiff is the president of the Royal Court and Court of Appeal (the Chief Justice), the president of the States Assembly (the national assembly), and the guardian of the constitutional privileges of the Bailiwick. He has no political functions or authority

What then are the fundamental framework conditions to justify long-term confidence in Jersey as a financial centre, and what are the challenges for us? The constitutional position is not, I think, material. Whether Jersey remains a Crown Dependency or claims at some future date sovereign status is not a relevant consideration. Any transition to sovereignty would be consensual and orderly. I take it as axiomatic that the political stability enjoyed for a very long time will continue. Our political institutions are democratic and mature and have shown a capacity to change and develop in a measured way. I take it as axiomatic that the government of Jersey will continue to maintain a fiscal framework that is attractive to investors, as it has done for more than 40 years.

I also mention for completeness the judicial independence that has existed for a long time. While Jersey's political autonomy is qualified, its judicial independence is complete. We have our own laws and judicial and legal system. I am often told that investors look for a mature judicial system in which they can have confidence. I naturally exclude your present speaker but the Court of Appeal also includes a number of very distinguished judges from the British Isles, and appeal lies from there to the Privy Council. The courts develop the law, in particular in relation to the administration of trusts, clarify the duties of trustees, and contribute to the certainty of investors that any disputes in relation to the administration of their assets will be will be fairly and speedily resolved. There is a professional system of law reports and the only law review, so far as I know, to be published in a small financial centre. The government has invested substantially in an online legal information system so that we have a website containing all the laws and regulations going back to 1771, all the judgments of the courts and other legal materials. Unusually, the revised laws of Jersey, that is an up-to-date statement of all statutory law, are available online free of charge to the public. Investors throughout the world, and their advisers, can therefore easily consult the website for



information as to the current laws and regulatory framework. It seems to me that all these framework conditions for investor confidence, political, legal and judicial stability, are self-evident and no more need be said.

I should mention the relationship of Jersey with Europe, although this cannot easily be disentangled from the constitutional relationship with the UK. The theory is simple. Jersey is not inside the European Union, and does not form part of the European Communities. The relationship is governed by a short and rather imprecise protocol, Protocol 3, to the 1972 Treaty of Accession of the UK to the European Communities. In broad terms the Bailiwick is outside the EC but inside for trade in goods and agricultural products, and forms part of the Customs Union. Of the four freedoms, only freedom of movement of goods applies to the Bailiwick. The protocol also contains a non-discrimination provision, which obliges us to apply the same treatment to all natural and legal persons of the Community. While the theory is simple, the reality may be a little more complicated, particularly since the Single European Act and, to an extent, the Maastricht Treaty. Directives sometimes have several treaty bases, which make it difficult to ascertain whether they relate to the freedom of movement of goods or not. But usually these problems of interpretation can be resolved. Jersey has no direct relationship with the European Commission, although our officials frequently have contact with different DGs. I believe that the Commission has a good understanding of the nature of the financial services industry in the Bailiwick and of the regulatory structure which is in place. For our part we try, through various sources, to keep up-to-date with changes in the making.

The legal relationship with Europe does not of course exclude the possibility, as we learned in 1998 or thereabouts, of being affected by political developments. The Tax on Savings Directive is the obvious example, but the Code of Conduct on Business Taxation was a more serious challenge. The process whereby member states were led to believe that the Crown Dependencies would adopt the Code left much to be desired. The underlying rationale was also of doubtful conformity with international law. The premise of member states is that, although taxation is a legitimate instrument of national economic policy in order to promote competitiveness, certain tax measures are inherently “harmful” and must be eliminated. It is true that other factors were in due course instrumental in persuading the government of Jersey to change the basis of its framework for the taxation of companies, but pressure from the EU and the UK was not insignificant. I want to return to this theme in due course.



Small states that do not observe international norms in terms of the regulation of economic activity and the suppression of drug trafficking, money laundering and other serious economic crime (including tax evasion) must of course expect an adverse reaction from the community of civilised nations. There must be effective regulation. Jersey is not of course in that position. The Bailiwick's compliance with international standards has been endorsed by the FATF and IMF. To the extent that this is possible, the regime in Jersey is based upon principle rather than the dogmatic application of inflexible rules. The object is to apply a common-sense approach to international standards. Standards are rigorously enforced, but they are proportionately and sensibly applied when it is clear that there is no risk of abuse, and that the standard needs to be tailored to the circumstances of Jersey. I give as an example the small and highly visible charities sector, where heavy-handed regulation would be disproportionate to the risk of money laundering posed by local charities and in some cases destroy the dedicated voluntary work of those engaged in numerous good causes.

I do not in any sense argue for a selective or cavalier approach to international standards. On the contrary I fully endorse their application in every small financial centre based upon a robust evaluation process such as the IMF evaluation process based upon the FATF 40 + 9 recommendations, the Basel, IOSCO and IAIS Core Principles and the FATF evaluation methodology. I do think however that the process should involve an assessment of risk in the jurisdiction in question, so as to reach a judgment that is sensible. The brain surgeon does not use knitting needles and standard kitchen knives – he uses instruments that are precisely matched to the operation being performed. There is otherwise a risk of clumsy over-regulation and, for small states, a disproportionate allocation of resources to problems that do not really exist. There is a standard below which all financial centres should not fall, but one should never lose sight of the purpose and object to which the regulation is addressed. That is “effective” regulation.

I will give one example from the experience of Jersey and some other small states for which the administration of trusts forms an important part of their financial services business. The assessment of risk led to an appreciation that some small businesses handling significant sums of money and complex investments might not meet the expectations of government in terms of, for example, the suppression of money laundering. Trust administrators and company service providers are accordingly regulated to standards set by the Offshore Group of Banking Supervisors. In Jersey a number of unsatisfactory operators have been weeded



out. There is, however, no internationally prescribed standard. Large jurisdictions such as the US and the UK, which also have significant trust business, do not assess the risk in the same way, and have no such controls. This seems to me to be a good example of the ways in which small states can play an active part in the debate on appropriate international standards.

If regulation is not to be a heavy hand, which discourages initiative and stifles competition, there must be a relationship between the regulator and those who are regulated. The controls on trust administrators and company service providers, which I have just described, were introduced with the broad support of the industry. All responsible businesses recognise the need to protect investors, (sometimes even from themselves), and to play their part in terms of international cooperation. What Jersey tries to do is to create a partnership between the regulator and those subject to regulation. It involves an approach which identifies risks that are specific to the jurisdiction, while at the same time allowing as much freedom to those who are in business as is consistent with the avoidance of that risk. If the regulator and the representative of lawyers, accountants, bankers and others are in accord, there is a strong probability that the government will react favourably to any legislative changes which are necessary to create the commercial opportunities. And this must be in the interests of investors. Innovation and fresh thinking, together with all those comfortable stabilities which investors need, are the ideal combination.

What then is the major challenge for a jurisdiction such as Jersey in maintaining the confidence of investors? The major challenge, in my view, is to defuse the antagonism towards small financial centres brought about by globalisation. One can understand that it is difficult in a world of freely flowing capital for a large economy to protect jobs, and to meet pension, health and welfare obligations. It is all too tempting for the elephant to stamp in frustration on the smaller and more agile animals on the jungle floor. Lip service is paid to tax competition, but the instincts of larger countries too often rebel against it. It is easier for large countries to attack the offshore centres than to face up to difficult choices and to explain them to their own citizens. It is easier to attach pejorative labels (e.g. tax havens, black holes of money laundering), to exaggerate and to foster myths than it is to face the reality of competition. This is of course unfair, but life is often unfair.



What can we do about it? The view taken in Jersey is that greater efforts must be made to dispel the myths. In fact, the standard of regulation in Jersey, and I use the term “regulation” to mean the supervision of licensed financial services providers but also the suppression of money laundering, terrorist financing and financial crime, is high, and in some respects higher than in some large countries. Large countries sometimes apply convenient double standards. Small states are occasionally driven to super-equivalence in order to persuade their critics that they indeed conform to international standards. Jersey and other responsible small states are cooperative and do respond positively to requests for assistance from those investigating serious crime. These are the messages which need to be hammered through to international organisations like the OECD and the EU and to the foreign departments of some larger countries. If one plays by the rules of the game one is entitled to expect equal treatment on the field of play.