

THE STATES OF DELIBERATION
of the
ISLAND OF GUERNSEY

POLICY & RESOURCES COMMITTEE

**MANAGING THE IMPLICATIONS FOR GUERNSEY BECAUSE OF THE UK'S CHANGING
RELATIONSHIP WITH THE EU**

The States are asked to decide:-

Whether, after consideration of the Policy Letter under the above title dated 27th June 2016, they endorse the Policy & Resources Committee to lead on the negotiations with the UK, in accordance with its mandate, in particular to:

- i. engage with the UK in the four main areas of concern outlined in paragraph 7.4;
- ii. seek to protect and secure the best interests of Guernsey in its trading relationship and for those resident in the Bailiwick;
- iii. to take all other necessary measures that may be considered appropriate; and
- iv. to note that the Policy and Resources Committee will undertake to keep States Members advised of progress.

The above Proposition has been submitted to Her Majesty's Procureur for advice on any legal or constitutional implications in accordance with Rule 4(1) of the Rules of Procedure of the States of Deliberation and their Committees.

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The Presiding Officer
States of Guernsey
Royal Court House
St Peter Port

27th June 2016

Dear Sir

1. Executive summary

- 1.1. The States of Deliberation is asked to reinforce the mandate of the Policy & Resources Committee to negotiate with the UK Government to seek to replace Guernsey's Protocol 3 relationship. This is following the outcome of the UK's EU referendum on 23 June 2016 after which it is expected to that the UK will formally notify the European Council of its intention to leave the European Union.
- 1.2. The Assembly is also asked to direct the Policy & Resources Committee to work to protect and secure the best interests of Guernsey and its residents, along with the other islands of the Bailiwick and the other Crown Dependencies.

2. Guernsey's relationship with the European Union

- 2.1. Guernsey is not part of the European Union. Guernsey neither contributes to, nor directly receives anything from, the funds of the European Union. However, there is a formal relationship between the Channel Islands and the EU which is governed by Protocol 3 to the UK's Act of Accession to the European Economic Community in 1972 ("Protocol 3") (Appendix 1). Over the ensuing 43 years, Guernsey has built up its own direct relationship with the EU, by voluntarily applying relevant EU standards and other forms of cooperation, which is separate from and additional to the formal Protocol 3 relationship through the UK.

2.2. Guernsey's relationship with the EU is managed with the assistance of the Channel Islands Brussels Office ('CIBO'). CIBO was established in 2011 to promote the interests of the Channel Islands in Europe, to represent the Channel Islands to the EU institutions, and to advise the governments of Guernsey and Jersey on EU policy issues. It is jointly funded by the States of Guernsey and the Government of Jersey.

2.3. Protocol 3

2.3.1. Under Protocol 3, Guernsey is part of the EU Customs Union and is able to trade in goods and agricultural products as if it were part of the EU. This means that trade is unrestricted by tariffs, quotas or other barriers (except VAT). Any traded products must meet the relevant standards and environmental requirements of the EU.

2.3.2. Protocol 3 also requires the Channel Islands to treat all natural and legal persons of the EU in the same way, which means that the Channel Islands cannot treat someone from the UK, for example, differently from someone from any other EU member state. However, Guernsey is not bound by other aspects of EU free movement rules and is able to maintain restrictions on the right to reside and work, in accordance with insular law, provided this is done in a non-discriminatory way.

2.3.3. Protocol 3 excludes "Channel Islanders" from the provisions allowing the free movement of persons. A person who was born (or who has at least one parent or grandparent who was born) in the UK, or who has resided in the UK for 5 years is not a "Channel Islander" for the purposes of Protocol 3 and enjoys free movement throughout the EU (including the right to work and reside).

2.4. "Third country" relationships

2.4.1. Outside of the formal Protocol 3 relationship, Guernsey is treated as a jurisdiction outside of the EU and one that is not a European Economic Area (EEA) country. This means it is treated as a 'third country'.

2.4.2. As a third country, and due to Guernsey's location and close trading relationships with both the UK and other EU member states, Guernsey voluntarily implements appropriate EU legislation and applies relevant international standards. Guernsey is not, for example, part of the single market in financial services and so has negotiated limited market access as a third country on a case by case basis by being assessed as applying equivalent standards to those in the EU. This includes in areas such as the Single European Payments Area ('SEPA'), the Alternative Investment

Fund Manager Directive ('AIFMD') and data protection. CIBO is actively engaged on the Channel Islands' behalf on a range of developing EU dossiers with the objective of securing third country interests for the islands.

- 2.4.3. By virtue of Guernsey's geographical location, it has also applied the relevant aviation and maritime measures to secure and underpin our transport links.

2.5. UK review of the balance of competences

- 2.5.1. In 2010, the Conservative-Liberal Democrat coalition agreement included a commitment to conduct a review of the balance of competences between the UK and the EU. This balance of competences review was carried out between 2012 and 2014 and was effectively an audit of what the EU does and how it affects the UK. The UK's review was extensive and submissions were received from the UK Parliament, businesses and business representative bodies, devolved administrations, civil society as well as the UK's European partners, EU institutions and other governments. The review did not produce specific recommendations but provided a general overview which would be relied upon for future reference.
- 2.5.2. The States of Guernsey, in conjunction with the States of Jersey and the Isle of Man Government, engaged with this review, coordinated by CIBO. Whilst the review of the balance of competences was not of the competences in relation to the Crown Dependencies, the islands collectively saw benefit in engaging in this review. This was in order to ensure the resulting reports, as a set of reference documents, included details of the islands' constitutional relationships and how EU competences impacted upon the islands, whether directly or indirectly. The review also provided the opportunity to ensure a good relationship was maintained with these UK Government Departments as well as to develop the UK Government's understanding of these issues. This will provide a good platform with which to engage with the UK Government in the negotiation on EU matters. The review concluded in December 2014 and as a result of this engagement, references to the Crown Dependencies can be found in many of the reports¹.
- 2.5.3. As well as building an understanding across Whitehall, the UK's review provided an opportunity for Guernsey to carry out its own informal review of how EU policy and legislation impacted on Guernsey and how any change in the UK's relationship might impact upon Guernsey.

¹ <https://www.gov.uk/guidance/review-of-the-balance-of-competences>

2.6. Guernsey's current position

- 2.6.1. The States of Guernsey has not been seeking to change its formal relationship with the EU. The current relationship is well understood and has served the test of time for all of the Crown Dependencies. In 2015, the External Relations Group of the Policy Council looked at the output of the balance of competences review in light of the impact that a UK exit might have and concluded there was no basis on which to suggest to the States that it should seek to change its relationship with the EU.

3. The UK's changing relationship with the European Union

- 3.1. Since the UK General Election held in May 2015 the UK Government has pursued an agenda of reform and renegotiation to deliver change in the UK relationship with the European Union, which was then put to the UK electorate in the first referendum on the UK's membership of the EU since 1975.

3.2. The UK's renegotiation

- 3.2.1. The Policy Council's External Relations Group and CIBO led engagement with the UK Government together with officials from Guernsey and Jersey in order to ensure that the islands were kept informed on progress on these reform negotiations. This helped to ensure that the Channel Islands' interests were understood and where appropriate taken into account. This engagement built upon the relationships developed with the UK Government during its balance of competences review.
- 3.2.2. The UK Government has kept the islands informed of its renegotiation objectives, at ministerial level through meetings with the Rt. Hon David Lidington MP, Minister of State for Europe, and at official level in the Foreign and Commonwealth Office, the Cabinet Office and the Ministry of Justice.
- 3.2.3. The UK Government concluded its renegotiation at the European Council meeting held on 18-19 February 2016². On 22 February 2016, the UK Government produced a white paper explaining the UK Government view of its reformed relationship with the EU entitled: "The Best of Both Worlds: the United Kingdom's special relationship status in a reformed EU".³

² <http://www.consilium.europa.eu/en/press/press-releases/2016/02/19-euco-conclusions/>

³ <https://www.gov.uk/government/publications/the-best-of-both-worlds-the-united-kingdoms-special-status-in-a-reformed-European-union>

3.2.4. The renegotiation deal covered the four main areas of reform sought by the UK: economic governance; competitiveness; sovereignty; and immigration. These reforms included:

Sovereignty

- Recognition that references in the EU Treaties to "ever closer union" would not apply to the UK and that the UK would not be committed to further political integration; and
- A "red card" system whereby a majority of national parliaments would be able to force a proposed piece of EU legislation to be withdrawn or substantially amended.

Economic governance

- Recognition that discrimination between firms cannot be based on the currency of a member state in which they are established. This may have helped prevent UK financial services firms being forced to relocate to the Eurozone in order to carry out euro denominated business); and
- An emergency safeguard for the UK (or other non-Eurozone country) to press the 'pause button' on the adoption of legislation relating to Eurozone banking union if it is believed that the proposed legislation will be detrimental to the integrity of the single market.

Immigration

- The option for member states to index child benefit to the level in the country of origin for the children of EU migrants living overseas whose children still reside in the country of origin. This would have applied immediately for new arrivals and from 2020 for existing claimants; and
- An "emergency brake" on migrants' in-work benefits for four years when there are "exceptional" levels of migration. Once triggered, the emergency brake would have been applied for migrants arriving for seven years.

Competitiveness

- A declaration recognising that the EU needs to improve its competitiveness, including by completing the single market in key areas such as services, digital and energy.

3.2.5. This legally binding decision would only have come into effect had the UK notified the EU that it had decided to remain in the EU after the referendum. As a result of the UK referendum result, and the decision to leave the EU which is expected to follow, this renegotiated status falls away. Had the deal been implemented it is

possible that the reformed status might have benefitted Guernsey, it being part of the sterling zone and as a third country provider of financial services and investment funds into Europe. For example, the reforms relating to economic governance were designed to protect the interests of the UK and other member states outside the euro, as the Eurozone pursues further integration. This included preserving the integrity of the single market for financial services. Similarly, the recognition of the need to make the EU more competitive should have made it more outward looking and open to foreign investment. However, these potential benefits will now never be tested because the renegotiated deal will not now take effect.

3.3. The UK's EU referendum

3.3.1. In May 2015, in the Queen's Speech, it was announced that a bill would be brought before Parliament in order to establish a legal basis for an EU Referendum should a negotiation of a new settlement for the UK in the EU be successful (the European Union Referendum Bill). The franchise for any referendum is set by the bill that underpins that referendum. It is for the UK Parliament to define the franchise in a referendum held in the UK.

3.3.2. The explanatory note that accompanied the European Union Referendum Bill referenced the franchise in respect of the Crown Dependencies, stating that:

*"The exclusion of the residents of the Crown Dependencies from the franchise is justified. The exclusion pursues the legitimate aim of confining the franchise to those citizens with a close connection to the UK: although residents of the Crown Dependencies are part of the UK for the purposes of nationality law, the Crown Dependencies are not part of the UK, and they have their own directly elected legislative assemblies, administrative, fiscal and legal systems and their own court of law. They are not represented in the UK Parliament. Further, unlike Gibraltar, the Crown Dependencies are generally not bound by EU law. The exceptions are customs rules, quantitative restrictions and levies, and other import measures in respect of agricultural products."*⁴

3.3.3. This understanding of the constitutional relationship accorded with the External Relations Group's understanding of the relationships. It was noted by the Group in June 2015 and the following statement was issued:

⁴ <https://www.gov.uk/government/publications/European-union-referendum-bill-European-convention-on-human-rights-echr-and-delegated-powers-memoranda>

Guernsey is not part of the UK, it is a dependency of the Crown and has its own directly elected legislative assembly, administrative, fiscal and legal system and its own courts of law. Guernsey's relationship with the EU is governed by Protocol 3 to the UK Act of Accession in 1973. The States of Guernsey does not contribute to the EU budget nor does it benefit from EU subsidies. Guernsey is not represented in the European Parliament.

As a result of this constitutional relationship Guernsey residents do not generally form part of the franchise for UK Parliament which is being proposed by the UK Government as the basis for any EU referendum. The UK Government is also proposing that the franchise will be extended to Commonwealth citizens in Gibraltar. The island's constitutional relationships with the UK and the EU are significantly different to those held by Gibraltar. Gibraltar is represented in the European Parliament.

Guernsey residents that are former UK residents may have a right to vote in the referendum if they have lived abroad for less than 15 years. There has been no move to date to extend the franchise to Guernsey residents generally. Given these complex relationships any move to do so would raise a number of constitutional issues to consider.

Should the UK seek to leave the EU it is likely that it would affect the relationship that Guernsey has with the EU under Protocol 3. The Policy Council, along with the States of Jersey, has been exploring the possible implications of a different relationship with the EU through the Channel Islands Brussels Office. We have also engaged closely with the UK on this matter including taking part in its review of the Balance of Competences.

The Policy Council will continue to engage with the UK, on a government to government basis, on this matter to ensure the UK is directly aware of the potential impact that any changes in the relationship might have on Guernsey and its residents, both in respect of any negotiations that will precede the proposed referendum and as a result of any action the UK seeks to make following the referendum.

- 3.3.4. Debate on the franchise at both committee and report stage in the House of Commons focused on the entitlement to vote for those aged 16 and over, the situation of EU citizens living in the UK, and of residents of British Overseas Territories and Crown Dependencies. One particular amendment (Amendment 50) related to extension to all Crown Dependencies. This was rejected by the UK Parliament. The resulting European Union Referendum Act received Royal assent on 17 December 2015.

- 3.3.5. On 4 May 2016, a petition to HM The Queen was made by three individuals, including one Guernsey resident, which was seeking extension for the franchise to all Crown Dependency residents was dismissed.
- 3.3.6. During the UK's EU referendum campaign the Policy & Resources Committee and its predecessor the Policy Council maintained its position that the UK's EU referendum was a matter for the UK. It also maintained the position that the States of Guernsey was not seeking to change its relationship with the UK and the island's best interests would be best served by preserving the current relationship with the EU - namely maintain our status as a third country save for allowing free movement of goods with the UK and the rest of the EU.
- 3.3.7. The referendum was held on 23 June 2016 on the following question: "*Should the United Kingdom remain a member of the European Union or leave the European Union*" with an option of a 'remain' or a 'leave' result. The result of this referendum was declared on the morning of 24 June 2016 with 51.9% (17,410,742 votes) of the electorate seeking for the UK to leave the EU, with 48.1% (16,141,241 votes) favouring remaining in the EU. The voter turnout was 72.2%.
- 3.3.8. Following the announcement of the referendum result the UK Prime Minister made a statement where he announced his resignation to take effect before the Conservative Party Conference in October 2016. He advised that "*A negotiation with the European Union will need to begin under a new prime minister, and I think it is right that this new prime minister takes the decision about when to trigger Article 50 [of the Treaty of European Union] and start the formal and legal process of leaving the EU.*"

4. Impact of the UK's exit from the EU on Guernsey

- 4.1. There is no precedent for a member state leaving the EU in its current form and the withdrawal means unravelling all the rights and obligations that the UK has acquired over its forty years of membership. This will include matters as diverse as access to the single market, the common policies on agriculture and fishing, access to structural funds for poorer regions and shared foreign policy, including joint action on sanctions.
- 4.2. Greenland left the EU's predecessor, the European Economic Community, in 1985 following the establishment of Home Rule from Denmark in 1979 and with permission of the member states at the time. However, its removal was limited due to

Greenland's connection to Denmark (it is treated as an overseas country in the EU Treaties).

- 4.3. On 29 February 2016, the UK Government published a white paper on "the process of withdrawing from the European Union"⁵. The rules for exit are set out in Article 50 of the Treaty on European Union and a two-year period is specified for the withdrawing state to negotiate a withdrawal agreement, starting from the date of the formal notification by the UK of its intention to withdraw. After a maximum of two years the EU Treaties will cease to apply to the UK and as a result, Protocol 3 will cease to exist. This period of two years may be extended if the UK and the EU agree unanimously to do so (i.e. with the agreement of all 27 remaining member states).
- 4.4. Following the result of the referendum the UK Government will need to formally notify the European Council of its intention to leave the EU.. This notification will start the two-year process set out in Article 50 of the Treaty on European Union. Following the UK Prime Minister's announcement from 24 June 2016 that it will be for his successor to decide when to trigger Article 50 it is not known at this stage when this formal process will commence or what timescale will be sought.
- 4.5. The eventual withdrawal agreement will need to set out the terms of the UK's withdrawal from the EU, covering issues such as any acquired ("grandfathered") rights of EU nationals residing in the UK and UK nationals residing in the EU, and the future of UK nationals working in the EU institutions. The provisions on grandfathering rights will be of relevance to Guernsey. In its white paper the UK Government stated that *"it is therefore probable that it would take an extended period to negotiate first our exit from the EU, secondly our future arrangements with the EU, and thirdly our trade deals with countries outside of the EU, on any terms that would be acceptable to the UK. In short, a vote to leave the EU would be the start, not the end, of a process. It could lead to up to a decade or more of uncertainty."*
- 4.6. In parallel to the negotiations on a withdrawal agreement, the UK and the EU will begin negotiations on the UK's future relationship with the EU, as a non-Member. Ideally the two sets of negotiations (on withdrawal and on the new relationship) would conclude at the same time. In reality, the negotiations on the new relationship could take much longer than the withdrawal agreement.
- 4.7. Given that the main impact upon the islands of the UK's exit from the EU means that Protocol 3 will fall away, it will be crucial for Guernsey to engage with the UK's negotiations in order to secure an equivalent access to the Customs Union and free

⁵ <https://www.gov.uk/government/publications/the-process-for-withdrawing-from-the-European-union>

movement of goods. The aim will be to prevent the introduction of trade barriers such as tariffs or qualitative restrictions. Guernsey's stand-alone relationships with the EU will not be substantially affected by the UK leaving the EU, however Guernsey will need to ensure it closely monitors the UK's negotiations to safeguard these third country relationships.

- 4.8. Appendix 2 ('Impact of a UK Exit on Guernsey - a Sectorial Analysis') provides a brief analysis undertaken by the Policy Council and CIBO during 2015 on the potential areas that Guernsey will need to closely monitor and engage with during the UK's renegotiation of a new relationship with the EU. In summary, the trade in goods to and from Guernsey is generally via the UK and therefore more dependent on free trade arrangements with the UK than the rest of the EU under Protocol 3. The trade in services with the EU is underpinned by Guernsey's third country relationships with the EU that are therefore not dependent on the UK's membership of the EU. These will not be impacted by the UK leaving the EU. There are more complex arrangements in relation to free movement of persons due to the constitutional links with the UK through the Crown. Those island residents that have certain EU rights, through the UK, will be impacted by any change in the UK's legislation and policies.
- 4.9. It is possible to envisage that the areas impacted by the UK's decision to leave the EU – in particular those provided for in Protocol 3 – may be replicated or replaced with some other agreement meaning that the island retains something akin to the status quo for Guernsey. The terms of this will be dependent on the alternative relationship that the UK seeks with the EU.

5. Economic impact

- 5.1. It is acknowledged that the UK exit from the EU may have an economic impact upon Guernsey, in the short term and the long term⁶. The UK Government has predicted a negative economic impact in the short and longer term. In May 2016, the International Monetary Fund assessment of the outlook suggested that: "a vote for exit would precipitate a protracted period of heightened uncertainty, leading to financial market volatility and hit to output"; "the long-run effects on UK output and incomes would also likely be negative and substantial"; and that "in the event of a Leave vote, policies should be geared towards supporting stability and reducing uncertainty"⁷. The IMF noted that concerns had already begun to affect UK markets in the run up to the referendum. This reflected the views of local industry who had noticed delays in investment and decision making before the referendum.

⁶ <https://www.gov.uk/government/publications/hm-treasury-analysis-the-immediate-economic-impact-of-leaving-the-eu>

⁷ <http://www.imf.org/external/np/ms/2016/051316.htm>

- 5.2. Given that Guernsey is in *de facto* monetary union with the UK, it is acknowledged that in May 2016 the Bank of England announced that it had plans for liquidity auctions in the weeks around the referendum to minimise adverse fiscal effects. If there is a longer term economic impact then measures to minimise the economic impact could be considered at that stage.
- 5.3. Economic uncertainty generally is a matter which is beyond the States' sphere of influence. However, by managing our relationship carefully we can minimise the uncertainty and ensure that we maintain confidence of industry. In this regard the policy of seeking to maintain the island's trading relationships in light of the UK decision to leave the EU ensures the States are doing what they can, as recommended by the IMF, to support stability, limit uncertainty and maintain confidence.

6. Alternative models for the UK relationship with the EU

- 6.1. On 2 March 2016, the UK Government published a white paper on "Alternatives to Membership: possible models for the United Kingdom outside the European Union"⁸. The UK Government has not assessed the benefits offered by any alternative model against membership of the EU. The UK Government has not announced what its preferred alternative might be and therefore any detailed analysis is based on speculation. However, the work of the Policy & Resources Committee (including its predecessor) and CIBO to analyse the alternative models is consistent with the UK Government's 'Alternatives to Membership' white paper. Some of the present options are summarised below.

6.2. Option 1: The UK joins the European Economic Area (EEA) (the "Norway model").

- 6.2.1. This would require the UK to accept all the EU's "*acquis communautaire*" (the EU body of law) across the four freedoms (goods, services, capital, people) and to make a contribution to the EU budget (though much less than now) without a seat at the negotiating table.

6.3. Option 2: The UK re-joins the European Free Trade Agreement (EFTA)

- 6.3.1. Given the development of the European Economic Area (EEA) agreement and of bilateral relations between Switzerland (the only European Free Trade Association country not in the EEA) and the EU, the main substance of the EU/EFTA agreement relates to trade in certain fish and agricultural products.

⁸ <https://www.gov.uk/government/publications/alternatives-to-membership-possible-models-for-the-united-kingdom-outside-the-european-union>

6.4. Option 3: The UK negotiates a series of agreements (the “Swiss model”)

6.4.1. Switzerland has over 120 agreements with the EU, although only one relates to financial services. The EU institutions are understood to regard the Swiss model as unsatisfactory, when compared to proper institutional framework along the lines of the EEA.

6.5. Option 4: The UK joins a customs union with the EU (the “Turkish model”)

6.5.1. Being in a customs union with the EU eliminates internal tariffs and requires the participating countries to agree on the EU Common External Tariff (CET). Under such arrangements the UK may be required to accept large sections of the EU *acquis* relating to manufactured goods and to competition policy. The Turkish model might not cover trade in services.

6.6. Option 5: The UK negotiates a free trade agreement with the EU (the “Canada model”)

6.6.1. A relationship with the EU which relies on a free trade agreement (FTA) would require the negotiation of favourable terms which will be influenced by the size of the British economy, the fifth largest in the world. It will also be influenced by the UK’s importance to the rest of the EU, over half of UK imports come from the EU. However, such an agreement would also be dependent on favourable political relationships. FTAs generally take a number of years to conclude and take effect. Most FTAs only provide for better market access than that provided by World Trade Organisation (WTO) rules rather than ‘free trade’.

6.7. Option 6: The UK does not conclude any trade agreement with the EU and relies on World Trade Organisation rules

6.7.1. The rules of the World Trade Organisation (WTO) rules set limits on the maximum tariffs that countries can apply to trade in goods. The EU and its member states would become third countries vis-a-vis the UK and vice versa. The WTO operates on the basis of the Most Favoured Nation (MFN) principle i.e. the benefit offered to one trading partner must be offered to all other WTO members (unless there is a preferential arrangement such as an FTA). It should be noted that in the event of a gap between the UK’s withdrawal from the EU and the entry into force of any new

agreement, and in the absence of any agreement on transitional measures, WTO provisions (only) would apply to trade between the UK and the EU.

- 6.7.2. The Policy & Resources Committee's predecessor the Policy Council had been giving ongoing consideration to asking the UK to extend its WTO membership to Guernsey. WTO membership would mean that Guernsey's exporters would face lower tariffs than is currently the case with Guernsey outside of the WTO. This work will need to be picked up by the Policy & Resources Committee in conjunction with the Committee *for* Economic Development during the course of this term of the States. In the long-term, Guernsey should keep open the option to become a full member of the WTO. The WTO rules allow for Guernsey to attain full membership but it would be a long and complex international negotiation process.

6.8. Option 7: The UK negotiates a bespoke agreement

- 6.8.1. The UK's unique situation as the first member state to withdraw from the EU may give rise to the possibility of the UK entering into a bespoke agreement, in a form which has not existed before. While possible, this is not considered in the UK Government 'Alternatives to Membership' white paper.

6.9. Guernsey's position in a new UK / EU relationship

- 6.9.1. Whilst the favoured option for a new UK / EU trading relationship is unknown it is difficult to plan with any certainty. Most of the options for the UK in terms of establishing a new trading relationship have a similar theme of including an option to allow for some limitation in barriers for trade in goods between the UK and the EU. The islands will be largely dependent on the UK in terms of how it will fit with that new UK / EU trading relationship. However, Guernsey has sufficient understanding of its own trading relations to input into that decision making and to inform how the island's interests may best be taken into account.
- 6.9.2. Guernsey's current relationship with the EU, until the UK has formally left the EU, is bound by Protocol 3 as being part of the EU treaties. The status and format of the new UK / EU relationship will determine to what extent any new trading relationship for Guernsey will also be 'hard wired' or whether there is any flexibility. The States may need to consider to what extent the relationship may be altered over time or whether any decision made at the outset of a new relationship will be binding and not subject to change.
- 6.9.3. Importantly, when the UK leaves the EU, the EU will no longer have the competence to enter into international trade agreements on the UK's behalf as is

currently the case under the Treaty of Lisbon. This will enable the UK to enter into new trade agreements of its own. This change may therefore provide new trading opportunities for Guernsey as it has been hitherto unable to extend EU trade agreements, except in so far as Protocol 3 applies. However, experience suggests that it is likely to take the UK many years to negotiate new trade agreements.

6.9.4. The objectives for the States to consider when negotiating with the UK are summarised in Appendix 4: Negotiating Objectives and Considerations.

7. Engagement with the UK

7.1. In negotiations leading up to the 1972 UK Accession Treaty and Protocol 3 the Channel Islands were excluded by the UK from the negotiations in Brussels, generally kept poorly informed of developments, and presented at various points with completed proposals. However, since that time the islands have become more outward looking and developed a greater international identity of their own, in accordance with the International Identity Framework document. The islands have also put considerable effort into engaging with the UK Government on the balance of competences review and to ensuring that we are kept informed of the progress in the reform negotiations.

7.2. Guernsey's broader engagement with the EU through CIBO has also helped secure much greater recognition than existed in 1972, including that:

- (a) the Channel Islands do have distinct interests that we need to protect;
- (b) the UK has a constitutional duty to help us to do so; and
- (c) this is best achieved by mature and regular consultation.

7.3. Whilst Guernsey has a greater identity of its own, it is expected that the UK is likely to want to deal with all three Crown Dependencies together and it will be important, as well as in each jurisdiction's interest, to resolve any differences that might arise prior to an approach to the UK. The islands should seek to present a package of agreed measures, settled between themselves, in order to strengthen the changes of securing the best possible outcome for the islands.

7.4. In order to ensure that Guernsey's interests are best served in the forthcoming negotiations with the UK it will need to ensure it monitors and engages with the UK Government to:

- (i) Ensure the interests of Guernsey residents are taken into account by the UK / EU exit agreement. This includes ensuring that Guernsey residents/persons

with EU rights do not suffer any detriment compared to those resident in the UK;

- (ii) Ensure, where possible, the arrangements for free movement of goods described in Protocol 3 are replicated in some way. This may be through extension of the relevant part of any new UK / EU relationship. The States should also ensure that the best interests of Guernsey residents and businesses are served under that new agreement;
 - (iii) Ensure there is no detriment to the existing, and historic, constitutional relationship between Guernsey and the UK. Explain and work to mitigate against any risks of unintended consequences; and
 - (iv) Seek opportunities for Guernsey in any new UK trading relationship including with the EU and with other countries outside of the EU, including any new free trade agreements and exploring extension of the UK membership of the WTO.
- 7.5. Given the likely huge pressures on UK Ministers and civil servants, the States will need to manage its engagement sensitively. It may be possible to seek to facilitate engagement with the Devolved Administrations, (while making clear that our constitutional position, and our relationship with the EU, is entirely different from the Devolved Administrations) as well as engaging collectively with the UK Government as the Crown Dependencies.

8. Engagement with the other islands of the Bailiwick and the other Crown Dependencies

- 8.1. The Policy & Resources Committee will need to ensure that there is continual liaison with the States of Alderney and the Chief Pleas of Sark at each stage of the UK's negotiation process. This will ensure that their interests are taken into account in order to seek a unified Bailiwick wide view. The Bailiwick Council will therefore serve as an important forum for discussion and consideration of any negotiations with the UK.
- 8.2. The States of Guernsey has closely engaged with the States of Jersey and the Government of the Isle of Man throughout the UK's review of the balance of competences and in the lead up to the referendum. All three governments recognise the importance of close co-ordination and alignment on the process for engagement with the UK's re-negotiation with the EU. Ongoing engagement with the authorities of

these islands will be enhanced in order to ensure timely and open dialogue during the process of negotiation and in order to pool resources and expertise. This will help ensure the best interests of each of the Crown Dependencies are best served.

9. Resource and implementation plan

- 9.1. Whilst it is unclear how exactly the Protocol 3 relationship will be replicated, there is confidence that working with CIBO and collaboratively with the other Crown Dependencies, the islands are well placed to secure arrangements that are in the best interests of the Bailiwick.
- 9.2. Because of the uncertainty around the detail it is unclear how much work this may require. Provisional estimates suggest that it may take two senior officers, with sufficient knowledge of EU matters in the Office *of the* Policy & Resources Committee to undertake the work. This does not take into account any additional discrete but related projects that may be required in the offices of the principal committees. Additional travel budget will also need to be allocated to ensure those staff are able to attend meetings in London and Brussels where necessary.
- 9.3. A proposal to part fund a member of staff to be seconded to London and shared between Jersey, Guernsey and the Isle of Man has been discussed, to be based at the Jersey London Office. Additional resource may also be required at the Law Officers' chambers to review legislation that has been implemented to comply with Protocol 3.
- 9.4. Additional work may also be required by CIBO, funded from existing budgets.
- 9.5. Every effort will be made to undertake this work with existing staff and in-house expertise, as well as expertise from bodies such as the Guernsey Financial Services Commission. Every effort will also be made to reprioritise existing budgets to meet as great a proportion of the costs as possible. However, the States are asked to acknowledge additional resources may be needed and it may not be able to be covered from reprioritising existing resources. Should extra resources and funding be required, more detailed proposals will be brought before the States if necessary.
- 9.6. It should be noted that the need to the prioritise States' resources to engage with the UK on the negotiations, combined with the UK Government's own resource implications as a result of the exit, will impact the ability to deliver other policy objectives. In particular where they require ongoing negotiation with the UK Government, for example projects such as the negotiation on the proposals of the Constitutional Investigation Committee agreed by the States in January 2016.

10. Engagement and consultation on these proposals

10.1. During the course of the UK's EU referendum the Office *of the* Policy & Resources Committee and the Office *of the* Committee *for* Economic Development, and their predecessor bodies, have been engaging with the businesses, industry bodies and other stakeholders. This engagement has been undertaken to ensure that the island's businesses were aware of the work that has been undertaken to date, the contingency planning and to discuss their interests and concerns. These ongoing discussions have been fed back into the contingency planning and will help inform the negotiations.

10.2. The publication of this Policy Letter provides the opportunity to continue this dialogue and widen the public engagement in this process.

10.3. The Office *of the* Policy & Resources Committee has also engaged with the relevant authorities in Alderney and Sark. It is acknowledged that this engagement will need to continue during the course of the renegotiations ahead. To date these authorities have been content with the proposals for seeking to maintain something akin to the status quo by replicating Protocol 3 in some way.

11. Propositions

11.1. The States are asked to endorse the Policy & Resources Committee to lead on the negotiations with the UK, in accordance with its mandate, in particular to:

- (i) engage with the UK in the four main areas of concern outlined in paragraph 7.4;**
- (ii) seek to protect and secure the best interests of Guernsey in its trading relationship and for those resident in the Bailiwick;**
- (iii) to take all other necessary measures that may be considered appropriate; and**
- (iv) to note that the Policy and Resources Committee will undertake to keep States Members advised of progress.**

12. Statement of support

12.1. In accordance with Rule 4(4) of the Rules of Procedure of the States of Deliberation and their Committees, it is confirmed that the propositions above has the unanimous support of the Policy & Resources Committee.

Yours faithfully

G A St Pier

President

L S Trott

Vice-President

A H Brouard

J P Le Tocq

T J Stephens

Appendix 1:
Protocol 3 to the UK Act of Accession of 1972

Article 1

1. The Community rules on customs matters and quantitative restrictions, in particular those of the Act of Accession, shall apply to the Channel Islands and the Isle of Man under the same conditions as they apply to the United Kingdom. In particular, customs duties and charges having equivalent effect between those territories and the Community, as originally constituted and between those territories and the new member states, shall be progressively reduced in accordance with the timetable laid down in Articles 32 and 36 of the Act of Accession. The Common Customs Tariff and the ECSC unified tariff shall be progressively applied in accordance with the timetable laid down in Articles 39 and 59 of the Act of Accession, and account being taken of Articles 109, 110 and 119 of that Act.

2. In respect of agricultural products and products processed there from which are the subject of a special trade regime, the levies and other import measures laid down in Community rules and applicable by the United Kingdom shall be applied to third countries.

Such provisions of Community rules, in particular those of the Act of Accession, as are necessary to allow free movement and observance of normal conditions of competition in trade in these products shall also be applicable.

The Council, acting by a qualified majority on a proposal from the Commission, shall determine the conditions under which the provisions referred to in the preceding subparagraphs shall be applicable to these territories.

Article 2

The rights enjoyed by Channel Islanders or Manxmen in the United Kingdom shall not be affected by the Act of Accession. However, such persons shall not benefit from the Community provisions relating to the free movement of persons and services.

Article 3

The provision of the Euratom Treaty applicable to persons or undertakings within the meaning of Article 196 of that Treaty shall apply to those persons or undertakings when they are established in the aforementioned territories.

Article 4

The authorities of these territories shall apply the same treatment to all natural and legal persons of the Community.

Article 5

If, during the application of the arrangements defined in this Protocol, difficulties appear on either side in relations between the Community and these territories, the Commission shall without delay propose to the Council such safeguard measures as it believes necessary, specifying their terms and conditions of application. The Council shall act by qualified majority within one month.

Article 6

In this protocol, Channel Islander or Manxman shall mean any citizen of the United Kingdom and Colonies who holds that citizenship by virtue of the fact that he, a parent or grandparent was born, adopted, naturalised or registered in the island in question; but such a person shall not for this purpose be regarded as a Channel Islander or Manxman if he, a parent or grandparent was born, adopted, or naturalised or registered in the United Kingdom. Nor shall he be so regarded if he has at any time been ordinarily resident in the United Kingdom for five years.

The administrative arrangements necessary to identify those persons will be notified to the Commission.

Appendix 2: Impact of a UK exit upon Guernsey - a sectoral analysis

a) Trade in goods, including agricultural and fisheries products

Guernsey's long-standing official position has been that it is not seeking any change to its formal relationship with the EU as set out in Protocol 3. On this basis at the outset of the UK's withdrawal agreement and new EU relationship it may be possible to be included in the scope of the provisions on trade in goods.

The volume of manufactured goods exported from the island is small. The majority of the importation of goods into the Channel Islands (including food, textiles, building materials and fuel) come via the UK. This means that the loss of Protocol 3 will have minimal direct effect on the island in terms of imports. This trade will be more dependent on there being free trade in goods arrangements between Guernsey and the UK. These arrangements predate Protocol 3 and are underpinned by rights described in the island's historic Royal Charters.

Almost all agricultural exports are to the UK, with a limited amount also exported outside the EU. However some of these goods are 'positional goods' of particular cultural significance to the islands. This underpins the importance of continued free access to the UK market.

In the case of fisheries it is estimated that about 80% of all fisheries products produced or caught in Bailiwick waters are exported or landed in France. This is often on the basis of price as well as logistical considerations.

With the end of Protocol 3, Guernsey fishermen would no longer have duty and quota free access to the French market. The fish would be treated as "third country" imports and be subject to higher tariffs and more onerous controls and checks. It could well make the exports uneconomic.

As we have seen in recent years, the application of Protocol 3 with respect to fisheries is contentious – the status of Channel Islands' fisheries vessels, whether or not UK quotas under the Common Fisheries Policy (CFP) apply to the Bailiwick vessels fishing in Bailiwick waters, and the application of certain EU rules.

It is not clear at this stage what agreement will govern UK relations with the EU on fisheries when the UK leaves, and the extent to which the UK – if no longer part of the CFP – could negotiate a "pure" trade agreement (for export/import of fisheries products hitherto covered by CFP rules).

The access of French fishermen to the British Fisheries limits appertaining to the Bailiwick of Guernsey is defined in the Fishery Limits Act 1964 (in accordance with the 1964 London

Convention) and access is limited by the Schole Bank agreement which would also remain in force.

b) Trade in services

Guernsey is a third country to the EU for financial services, with market access achieved on a case by-case basis through the “equivalence” process. This will therefore remain unchanged when the UK leaves the EU. The States will need to consider what the political impact of a UK exit from the EU might be in terms of any new market access negotiations and how the process might differ, in particular in respect of the how the UK might approach its own negotiations might operate. This will not be clear until the terms of any new UK / EU relationship are negotiated.

The biggest impact on Guernsey’s financial services industry will be indirect rather than direct – the effect of the UK exit from the EU might have on the UK economy in general and the City in particular. The IMF’s assessment of the economic impact was published on 13 May 2016⁹ and HM Treasury’s analysis of the economic impact of the UK leaving the EU was published on 23 May 2016.¹⁰

c) People

Since the islands are subject to UK Immigration and Nationality Laws, the States will not be able to negotiate anything directly with the EU relating to movement of persons. However, there will be a number of aspects of the UK exit negotiations which may impact upon us.

The States will need ensure the UK Government is aware of these issues and ensure that the insular authorities are regularly briefed on the progress of negotiations in this area. These issues may include:

- (i) ensuring that we are consulted prior to any commitments made by the UK as part of the UK exit agreement with respect to the grandfathering of rights of EU (non-UK) citizens in the UK and in the Channel Islands;
- (ii) ensuring that any ‘grandfathering’ of rights of British citizens in the rest of the EU as part of the UK exit agreement is broad and takes into account “Channel Islanders” as defined in Protocol 3;
- (iii) understanding whether the UK exit agreement will impact on the EU (non-UK) diaspora communities in Guernsey, taking account of any acquired rights under insular law; and

⁹ <http://www.imf.org/external/np/ms/2016/051316.htm>

¹⁰ <https://www.gov.uk/government/publications/hm-treasury-analysis-the-immediate-economic-impact-of-leaving-the-eu>

(iv) understanding whether the UK exit agreement includes any commitment by the UK regarding non-discrimination between nationals of different EU member states in any amendments to the immigration regime and how these might apply in the islands.

**Appendix 3:
Negotiating Objectives and Considerations**

a) Negotiating considerations - relationship with the UK

- (i) For trade in **goods**, including agriculture and fisheries products, there is a long-standing historic trading arrangement which provides for tariff-free reciprocal trade.
- (ii) There are no arrangements in place that make reference to trade in **services**, including financial services.
- (iii) For **people**, the Common Travel Area should continue to apply (it predates UK Accession, and is not dependent on EU law).

b) Negotiating objectives: relationship with the EU

- (i) In order to maintain the status quo for Guernsey, the States of Guernsey will need to maintain the free **trade in goods** with the EU hitherto provided under Protocol 3. In principle, it is possible that this may be replaced by extending the goods provisions of any new UK/EU agreement to Guernsey, subject to the precise terms.
- (ii) The existing work exploring extension of the UK **membership of the WTO** extended to them should be given a higher priority. This will provide lower tariffs for any imported goods coming direct from the EU or elsewhere (not via the UK) and will underpin an agreement on free movement of goods as well as other trading relationship.
- (iii) For **trade in services**, the States will seek to maintain its current position of being outside the EU, with market access on a case by case basis as third countries.
- (iv) For **people**, the States will need to seek to ensure any commitments made by the UK as part of its withdrawal agreement with respect to the grandfathering of rights of EU (non-UK) citizens in the UK and in the Channel Islands and that the legal status 'Channel Islander' (for the purposes of Protocol 3) are considered.

Appendix 4:

Main areas for engagement with the UK Government for the States of Guernsey

In order to ensure that Guernsey's interests are best served in the negotiations with the UK it will need to ensure it monitors and engages with the UK Government to:

- (i) ensure the interests of Guernsey residents are taken into account by the UK / EU exit agreement. This includes ensuring that Guernsey residents/persons with EU rights do not suffer any detriment compared to those resident in the UK;
- (ii) ensure, where possible, the arrangements for free movement of goods described in Protocol 3 are replicated in some way. This may be through extension of the relevant part of any new UK / EU relationship. The States should also ensure that the best interests of Guernsey residents and businesses are served under that new agreement;
- (iii) ensure there is no detriment to the existing, and historic, constitutional relationship between Guernsey and the UK. Explain and work to mitigate against any risks of unintended consequences; and
- (iv) seek opportunities for Guernsey in any new UK trading relationship including with the EU and with other countries outside of the EU, including any new free trade agreements and exploring extension of the UK membership of the WTO.

(Replicated from para 7.4 of the Policy Letter for ease of reference)