



Isle of Man
Government

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Council of Ministers

UK referendum on EU membership Implications for the Isle of Man

First Interim Report

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Cabinet Office

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1 – Chief Minister’s Foreword

The Conservative Party’s 2015 election manifesto contained a pledge to renegotiate the terms of the United Kingdom’s membership of the European Union and then hold an ‘in/out’ referendum before the end of 2017.

Following the election of a Conservative majority Government, these negotiations began in earnest in the summer of 2015. After months of talks, EU leaders agreed a package of reforms on 19th February 2016, and the following day, the Prime Minister confirmed that the referendum would be held on Thursday 23rd June.

Although the Isle of Man is not part of the EU, nor is it included within the UK’s membership of the EU, it does have a very close relationship with the UK and also, through the UK, a limited relationship with the EU, which is set out in Protocol 3 to the UK’s Treaty of Accession.

This means that although the Isle of Man cannot influence the outcome of the referendum, it may be affected, should the UK vote to leave the EU – what has come to be known as ‘Brexit’.

This report sets out the potential impact on the Island of -

- the UK’s reformed membership of the EU, should the UK vote to remain in the EU;
- the effects of ‘Brexit’, should the UK vote to leave the EU; and
- also provides an overview of the potential ‘post Brexit’ scenarios

Much has been said and written on both sides of the referendum debate, and it is almost impossible to predict what the true effects of UK withdrawal will be, and even more difficult therefore, to say with any certainty at this time, what the impact on the Isle of Man will be.

It is important, however, that we set out how the existing relationship functions and explore which areas of our economy may be most affected by a UK withdrawal. It is also necessary to set out what is important to the Isle of Man, so we may be clear if and when negotiations begin for new ‘post-exit’ withdrawal agreement between the UK and EU, where the Isle of Man would wish to position itself.

If the UK does vote to leave, then there will be a period of at least two years while a withdrawal agreement is negotiated. It is highly likely that this will not only set out how the withdrawal will be carried out, but also the nature of the UK’s new relationship with the EU.

There is to be a general election in the Isle of Man in September 2016. It is likely, therefore, that in the event of a UK withdrawal from the EU, a new relationship for the Isle of Man would be negotiated during the course of the next administration.

Hon Allan Bell, MHK
Chief Minister

2 – Executive Summary

The Isle of Man is not part of the EU, but it does have a limited relationship with it, which is set out in Protocol 3 to the UK's Treaty of Accession. The Protocol allows for the Isle of Man to trade freely with the EU in manufactured goods and agricultural products

Even though the Isle of Man is not part of the EU, the result of the forthcoming referendum in the UK may affect the Island. The Council of Ministers has prepared this report which sets out how the Island may be affected by a vote to remain, and more importantly, by a vote to leave the EU.

Much is unknown at this stage. It is not possible to be sure what the exact impact will be, until it is known what new relationship the UK will negotiate with the EU.

The UK's reformed membership of the EU

The UK Government has negotiated a number of reforms which will only come into force, if the UK votes to remain in the EU. These are –

- Sovereignty – the UK will no longer be bound by the commitment to 'ever closer union', and there will be a provision to allow for National Parliaments to hold up EU legislation – if 55% of Member States are opposed
- Currency – there will be formal recognition that the Euro is not the only currency of the EU, that measures should not be taken to undermine other currencies, and also that non-Euro currencies should not have to pay for Eurozone bailouts
- Regulation & red tape – these are to be reduced and measures to increase competitiveness and employment enhanced
- Benefits – an emergency brake can be applied which will allow for restrictions to be put in place in respect of access to certain benefits, and also, some measures to reduce the level of child benefit if it is paid in respect of a child who lives outside the UK, where the standard of living is lower than that in the UK

The referendum

The referendum process is set out in UK legislation. The European Referendum Act received Royal Assent on 17 December 2016 and the referendum date is set for Thursday 23rd of June. Recent polling has fluctuated between both outcomes, and polling variables make the outcome difficult to predict.

The Electoral Commission designated on 13 April 2016 'Vote Leave' and 'Britain Stronger in Europe' as the official Leave and Remain campaigns in the forthcoming referendum. Isle of Man residents will not vote in the referendum, although those who qualify to vote in UK general elections – perhaps because they have lived in the UK recently – may do.

Residents of Gibraltar can vote, because unlike the Isle of Man, Gibraltar is included within the UK's membership of the EU.

Implications of a vote to 'remain'

If the UK votes to remain in the EU, then the terms of its new reformed membership will come into force. These reforms will not affect the Isle of Man. Protocol 3 will be unchanged and the reforms do not touch on areas which directly affect the Island.

Implications of a vote to 'leave'

If the UK leaves there will be an impact in a number of different areas, and these are covered in more detail in the report, but in summary they are as follows –

Constitutional and legal effects

Protocol 3 will fall away. The Protocol is attached to the UK's Accession Treaty – and is not part of the EU Treaty itself.

Article 50 of the Treaty sets out how a Member State can leave the EU, and allows for a two-year window within which the departing Member has to negotiate its 'withdrawal agreement' (although this can be extended).

It is anticipated that the UK's 'withdrawal agreement' would set out its new relationship with the EU, but the UK Government has stated that this could take up to ten years to resolve.

The Isle of Man's underlying relationship with the Crown and the UK would not change.

Free movement of goods and customs matters

Customs Union and currency union with the UK would continue, although the Customs and Excise Agreement may need to be amended, because it is written in a way that depends on UK membership of the EU (and references EU rules).

Trade with the EU and the rest of the world – for businesses both in the UK and the Isle of Man – could be disrupted.

Free movement of people

Manx residents who currently qualify as British Citizens would continue to do so, and British Citizens would continue to be able to live in the UK.

However, the rights of British Citizens to live and work in the rest of Europe may be affected. Similarly, the rights of EU citizens to live in and work in the UK and Isle of Man may also be affected.

Economic impact

Exporters of goods – that is those in the manufacturing, agricultural, and fisheries sectors – would be likely to see the most significant effect, as the Island's current relationship with the EU allows for free trade in these sectors.

Most food produced in the Isle of Man is exported to the UK but exports to the EU (either directly, or through UK intermediaries) and the rest of the world may see increased costs or

restrictions (higher tariffs or quotas) and administrative burden. Manufacturers may also see increased costs, barriers to trade or other non-tariff measures which could mean that their products are comparatively more costly. Their UK based partners could be similarly affected.

Aircraft, shipping and yacht management sectors may be adversely affected by changes to access to the European Market, and in particular if the Island's VAT status is altered. This could in turn affect the Corporate Service Providers who support this sector.

For Financial Services (and services generally), the Isle of Man is already classed as a 'third country' and so Island companies do not enjoy automatic right of access to the Single Market. For this reason, the UK leaving the EU is not anticipated to be likely to have a significant impact, although any impact on the UK would undoubtedly affect local businesses.

Similarly, e-gaming is not currently regulated at an EU level, with access to EU markets governed by national rules – this is unlikely to be significantly affected, but loss of UK influence in the EU could affect future policy in this area, and potentially restrict access to the EU market.

Provision of Government services

The delivery of Government services such as Health, Education and Home Affairs, and the many other services provided for the public will be largely unaffected.

Alternatives to EU membership

There are several possible models the UK may follow, should it vote to leave the EU. These include –

- Joining the EFTA (European Free Trade Area) and signing the EEA (European Economic Area) Agreement in order to remain inside the Single Market, like Norway
- Negotiating several bilateral agreements with the EU, like Switzerland
- Concluding a modern Free Trade Agreement with the EU, like Canada
- Entering into Customs Union with the EU, like Turkey
- Or none of these, and instead, relying on World Trade Organisation rules

It's not clear which the UK would be likely to pursue, although the EFTA/EEA and the WTO options seem least likely.

What is clear is that the Isle of Man is not entirely free to choose its own relationship with the EU. Because the Isle of Man is not sovereign it can't join the EU in its own right and can't join EFTA, nor negotiate an Association Agreement with the EU, as Andorra, Monaco and San Marino are doing.

The Isle of Man's options will be limited by the UK's eventual position. Subject to the agreement of the UK, and of the EU, the UK's withdrawal agreement may extend to include the Isle of Man in total, or in part, or not at all. How this would be done, from a legal perspective is not clear – and it won't be until the talks begin on the UK's withdrawal agreement

The Devolved Administrations

The Governments of all of the Devolved Administrations are in favour of the UK remaining in the EU. They, however, will be bound by the decision of the UK as whole, and of the UK's eventual settlement with the EU.

They may, of course, choose to seek independence from the rest of the UK. The Scottish First Minister has indicated that a vote to leave the EU could trigger a second independence referendum.

Conclusion & next steps

Isle of Man Government will use its first interim report as the basis for further political engagement and discussions with UK on mechanics of the negotiations, setting out the Isle of Man's position.

Discussions will be held with the other Crown Dependencies, to understand their respective positions.

Further consideration will be given to the impact on local business, as well as the potential effects of each the models for the UK's new relationship with the EU, should it vote to leave.

3. – Introduction

The purpose of this Report is to set out the effects on the Isle of Man of the renegotiation by United Kingdom ("UK") of the terms of its membership of the European Union, to provide an outline of the referendum process which is due to take place on 23rd June, and depending on the result, to assess the potential implications for the Island of the UK remaining in or leaving the European Union ("EU").

There are, however, many significant unknowns – the result of the referendum is not yet known, and its implications are the subject of fierce debate in the UK.

The Report, therefore, is broken into three main sections.

Firstly, there is a discussion of the reforms which the UK has succeeded in negotiating, and the impact they will have on the Isle of Man. It is worth noting that they come into force only in the event of a vote for the UK to 'remain' in the EU.

Secondly, there is an assessment of what would happen if the UK was to leave the EU, and the Island's own limited relationship with the EU, which is through the UK, was also to fall. This includes a discussion of the constitutional and legal effects, the impact on the free movement of goods and of people, an overview of the economic impact (sector by sector) and the effects on the effective delivery of Government services.

Thirdly, there is a discussion of the possible options for a new relationship for the UK with the EU, and what these may mean for the Island, along with the constitutional implications for the UK as a whole, should there be a vote to leave.

There is to be a general election in the Isle of Man in September 2016. If there is to be a new relationship between the Isle of Man and the EU, that will be negotiated under the new administration.

In addition, the report, as far as is possible at this stage, provides some useful information for those Isle of Man residents who may be entitled to vote in the referendum, and wish to understand the potential impact of their decision may have on the Island.

Finally, should there be a vote to leave on 23rd June, there will be an expectation that the negotiations for a new relationship will begin very quickly. This Report also, therefore, provides a basis for engagement with UK Government both prior to that vote, and immediately after it, so that the Island's needs are understood and accommodated.

The renegotiation & referendum process – an overview

1 – Renegotiation

Since the UK joined the EU in 1973, it has had an unsettled relationship with its EU partners. A referendum on continued membership was held in 1975, and since the completion of the Single Market in the 1980s, there has been growing unease with the process of deepening economic and political integration.

Although the UK has over a number of years secured a number of opt-outs and special arrangements – including non-participation in the Eurozone, in the Schengen border-free area, and some Justice and Home Affairs provisions – there continued to be a significant amount of frustration and mistrust amongst the British political establishment, some parts of the business community and the general public with the direction taken by the EU.

The successes of the UK Independence Party on an anti-EU platform, a predominantly Eurosceptic press and an increasing number of MPs within the Conservative Party calling for the UK to leave the EU, culminated with the Conservative Party including a commitment in its 2015 election manifesto to renegotiate the terms of UK's membership of the EU and hold an 'in/out' referendum before the end of 2017. The manifesto set out a number of areas for renegotiation, although they were at that stage, relatively broad and ill-defined.

The renegotiation process

Following the election of a majority Conservative Government, negotiations began almost immediately, with the Prime Minister and other senior politicians holding talks with their counterparts over the summer and autumn of 2015. Little detail or clarity emerged during the course of these negotiations, however, and European partners requested that the UK's wishes be set out clearly, so that meaningful discussion could begin.

The Prime Minister's proposals

The Prime Minister set out concrete proposals in a speech given at Chatham House on 10th November, and these were reproduced in a letter sent to Donald Tusk, President of the European Council on the same day¹.

These proposals were: –

Economic Governance

The UK wished it to be recognised and formally set out that the Euro is not the only currency used in the EU, and that whilst not wanting to stand in the way of further Euro-area integration, by the same token, non-Euro Member States should not be disadvantaged.

Specifically, the UK Government wanted to see recognition that –

- The EU has more than one currency

¹ <https://www.gov.uk/government/speeches/prime-ministers-speech-on-europe>

- There should be no discrimination and no disadvantage for any business on the basis of the currency of their country
- The integrity of the Single Market must be protected
- Any changes the Eurozone decides to make, such as the creation of a banking union, must be voluntary for non-Euro countries, never compulsory
- Taxpayers in non-Euro countries should never be financially liable for operations to support the Eurozone currency
- Just as financial stability and supervision has become a key area of competence for Eurozone institutions like the ECB (European Central Bank), so financial stability and supervision is a key area of competence for national institutions like the Bank of England for non-Euro members
- And any issues that affect all Member States must be discussed and decided by all Member States

Competitiveness

The UK affirmed its support for the EU Commission's current focus on supporting economic growth scaling back on regulation, as well as plans for a Capital Markets Union, which would boost funding and investment for EU businesses.

The UK also supported the Commission's new trade strategy to encourage massive trade deals with the US, China, and Japan.

The proposals in this area also concerned a commitment to cut the total burden on business and to make a clear long term commitment to cut regulation and boost investment and growth, removing barriers further to support the development of the Single Market.

Sovereignty

Specific requests in this area included –

- To end Britain's obligation to work towards 'ever closer union'
- An enhanced role for national parliaments, including the ability for a group of parliaments to veto EU legislative proposals
- Full commitment and adherence to the principle of subsidiarity (i.e. Europe where necessary, national where possible)
- And recognition and protection of the UK's existing opt-outs in the area of Justice and Home Affairs

Immigration

Emphasising that the UK is not opposed to the fundamental principle of free movement, it stressed that there is a problem for the UK in terms of the speed and scale of immigration into the UK currently and therefore proposed –

- When new countries are admitted to the EU in the future, free movement will not apply until their economies have converged much more closely with existing Member States
- A crack down on abuse of free movement, including tougher and longer re-entry bans for fraudsters and people who collude in sham marriages
- People coming to the UK from the EU must live there and contribute for four years before they qualify for in-work benefits or social housing

- An end to the practice of sending child benefit overseas

Tusk letter

Following receipt of the UK's proposals, the President of the European Council, Donald Tusk, set them out in a letter to the Member States of the EU, for discussion at its Summit of Heads of State and Government, to be held in December 2015².

The December Summit did not make much progress on the proposals and further discussion was consequently scheduled for a European Council meeting in February 2016. In the meantime, the EU and UK negotiators continued discussions and the Prime Minister embarked on further talks with EU governments.

On 3 February 2016 the European Council President Donald Tusk published six draft documents intended to address UK concerns. These were the basis for intensified negotiations with a view to reaching agreement in February 2016.

The Prime Minister continued to meet with his counterparts across the EU, and in mid-February, prior to the Summit itself, the President of the European Council tabled draft documents for discussion at the Summit.

European Summit February 18th and 19th 2016

The discussions were lengthy, and continued through the night of 18th February, with the final clean text – ready for agreement – emerging only towards the end of the second day of the meeting.

Overview of declarations

The key features of the deal secured by the UK were as follows –

Child benefits – there would not be, as the Prime Minister had originally hoped, a ban on the sending overseas child benefits, claimed in respect of children who live outside the UK. In the face of opposition from some of the Member States of Eastern Europe, there was agreement to allow the UK Government to pay child benefit to migrant workers with children in their home country at the rate of the cost of living in the child's home country. This would apply to new entrants, and to the existing 34,000 claimants from 2020.

In-work benefits – the UK would be entitled to apply for the introduction of a so-called 'emergency brake' to limit access to in-work benefits for EU migrants during their first four years in the UK. The UK would have to demonstrate that there was an 'exceptional' level of migration to the UK, and the brake could only be applied for seven years. The application of this 'emergency brake' would also be subject to the approval of the European Parliament, as well as a 55% majority in the European Council. (It is worth noting that there is some

² http://www.consilium.europa.eu/en/press/press-releases/2016/02/02-letter-tusk-proposal-new-settlement-uk/?utm_source=dsms-auto&utm_medium=email&utm_campaign=Letter+by+President+Donald+Tusk+to+the+Members+of+the+European+Council+on+his+proposal+for+a+new+settlement+for+the+United+Kingdom+within+the+European+Union

speculation that the 'emergency brake' could violate certain EU treaties, and therefore open up the possibility that it could be challenged in the European Court of Justice).

Eurozone – there would be official recognition of the pound as a currency within the EU, and measures to protect non-Eurozone countries against discrimination within the Single Market. Furthermore, there were assurances that the City and its large financial institutions will have safeguards to prevent Eurozone legislation being imposed on them, as well confirmation that supervision of national banks and markets will remain under the jurisdiction of UK regulators.

Competitiveness – an assurance that the EU Member States and institutions will continue to work together to improve the Single Market and cut red tape.

Ever closer union – the UK is not committed to be part of 'ever closer union' with the other Member States.

National Parliaments – 'Red card' – National Parliaments (55% threshold) can cause EU legislation to be halted, and redrafted in order to take account of their views.

Security – The UK can stop suspected terrorists and other criminals from entering the UK, even if the threat is not 'imminent'. There will also be new rules to close some loopholes including sham marriages.

What is the significance of the UK deal?

For the UK, the political significance of the deal could be said to outweigh the economic or constitutional/legal impact. The Prime Minister sought and obtained compromises which he hopes will go some way to addressing the interests in the City/financial services industry over the continued integration within the Eurozone, of the electorate in terms of immigration and access to benefits, and some within the Conservative Party concerning the role of national parliaments (sovereignty).

However, whether the restrictions on child benefit and access to in-work benefits will save money, or indeed deter inward-migration will remain to be seen. In addition, exemption from the concept of 'ever closer union' could be said to reflect the UK's existing position (outside the Eurozone, Schengen and many of the Justice of and Home Affairs provisions).

The willingness to provide these concessions does, however, show that EU Member States do want the UK to remain within the EU. It has, however, led to fears in several other countries that these reforms/compromises will lead other Member States to seek similar deals and carve outs in the future.

What does the new deal mean for the Isle of Man?

For the Isle of Man, the reforms do not alter the Island's underlying relationship with the EU, as Protocol 3 is not affected. The individual elements of the settlement will have little or no direct impact on the Island. The provision of benefits for EU (or any) migrants to the Island is not covered by EU rules (see section 9 below), other than the obligation to treat all EU nationals equally. Isle of Man rules already restrict access to benefits to those who can

demonstrate that they qualify as an 'Isle of Man worker', the definition of which is broadly similar to those requirements for work permits. Similarly, to qualify for child benefit, the child in question must have been resident in the Isle of Man for 26 out of the previous 52 weeks, at the time of the claim.

Finally, it must be noted that the new relationship will only come into force should the UK vote to remain in the EU.

2 – The Referendum

The European Union Referendum Act received Royal Assent on 17 December 2015, and provides that the Referendum must take place no later than 31 December 2017.

Several contentious issues emerged during the course of its debate.

Firstly, the referendum question itself was rephrased to allow for UK voters to state whether they wished the UK to 'remain' in the EU, or 'leave'. A straightforward 'yes' or 'no' answer to the question as to whether the UK should be a Member of the EU was felt to have more negative connotations.

Secondly, there was the question of the franchise. Moves to extend the vote to include 16-18 year olds were defeated by the UK Government, as were the proposal to include British Citizens living overseas, other than those who had retained their right to vote in UK general elections.

Thirdly, in relation to the issue of so-called 'purdah', a number of Conservative rebels forced the inclusion of a provision to ensure that the Government – including UK Civil Servants – could not actively campaign for the UK to remain in the EU, in the period immediately before the Referendum. Whilst there are certain provisions which allow for Government Ministers to continue day-to-day EU business, purdah rules will reduce the Government's ability to campaign in the lead up to the referendum.

The Electoral Commission

Although the campaign was effectively begun before Christmas, the announcement of the referendum date on 20th February acted as a trigger for the Electoral Commission. On 13 April 2016 the Electoral Commission designated 'Vote Leave' and 'Britain Stronger in Europe' as the official Leave and Remain campaigns for the forthcoming referendum. This designation will include higher spending limits, access to certain publicly funded grants, and opportunities for public broadcasts. This announcement is expected to introduce further clarity into the referendum debate.

'Leave' – the 'Vote Leave' campaign, led by former Chancellor of the Exchequer (during the Government of Margaret Thatcher) Lord Lawson, has attracted the support of some of the more prominent figures in the Conservative Party who are campaigning to leave the EU, including Boris Johnson, Iain Duncan Smith, Michael Gove and Priti Patel. It also has cross-party support; and the Conservatives for Britain Group has aligned itself with the 'Vote

Leave' campaign. 'Grassroots out' was formed following the split from the 'Vote Leave' campaign of the 'Leave.EU' group, which has the support of Nigel Farage and Labour's Kate Hoey MP.

'Remain' – 'Britain Stronger in Europe' was launched in October 2015, and is led by former Marks and Spencer Chairman Lord Rose. Labour and the Conservatives have also launched official campaigns to remain in the EU.

The referendum process – irrespective of the outcome – is likely to cause significant political and economic turbulence in the UK. Financial markets are likely to be unsettled, and it is also reported that many large international businesses are delaying investment decisions until the outcome of the referendum is known.

In addition, with the Devolved Administrations largely in favour of remaining in the EU, the potential vote to leave raises the prospect of a further referendum on Scottish Independence. (This is discussed in further detail at section 11).

IOM residents

Isle of Man residents are not permitted to vote in the EU referendum, as the Isle of Man is not a part of the UK, and the UK's membership of the EU does not extend to cover the Isle of Man and the Channel Islands as it does with Gibraltar. (Gibraltar is included within the UK's membership of the EU, although exempted from Customs Union/VAT, and the Common Agricultural Policy. It is, as with the UK, not a part of the Schengen area. To this extent, its relationship with the EU is almost the opposite of the Isle of Man's, which is set out in more detail in Section 3 below).

Former residents of the United Kingdom now living in the Isle of Man – who have been registered to vote in a UK constituency within the last 15 years – will be eligible to vote in the Referendum.

(Further information including how to register to vote is available on the UK Electoral Commission's website <http://www.electoralcommission.org.uk/i-am-a/voter/registering-to-vote-and-the-electoral-register>)

4 – Constitutional & legal issues

Background/context

The Isle of Man is a Dependency of the British Crown, with Her Majesty The Queen as Sovereign. The Sovereign is personally represented in the Island by the Lieutenant Governor. The Isle of Man is not part of the United Kingdom and is internally autonomous and self-governing, with its own, independent legal, administrative and fiscal systems. The Island's parliament, Tynwald, legislates for the Island.

UK legislation and international treaties are only extended to the Island with the prior consent of the Isle of Man Government.

The Isle of Man is not part of the EU or EEA but is in the Customs territory of the EU by virtue of Protocol 3 to the UK's Act of Accession 1972. This means that the Isle of Man can benefit from free movement of manufactured goods and agricultural products. The Island is also part of the Common Travel Area (CTA), along with the UK and the Republic of Ireland, which permits movement without immigration controls for all CTA nationals.

Within HM Government, the Ministry of Justice is the point of contact for the Crown Dependencies, and communications in both directions are passed through its offices.

Part XI of Volume 1 of the Report of the Royal Commission on the Constitution, published in 1973 and known as the Kilbrandon Report, sets out an account of the duties of the Crown in relation to its Dependencies. The Crown's responsibilities include:

- ultimate responsibility for the "good government" of the Islands (meaning the Isle of Man and the Channel Islands comprising the Bailiwicks of Jersey and Guernsey);
- the ratification of Island legislation by Order in Council (Royal Assent) following scrutiny by the relevant Privy Councillor (at the time of the Kilbrandon Report the Home Secretary, now the Justice Secretary);
- international representation, subject to consultation with the insular authorities prior to the conclusion of any agreement which would apply to them;
- ensuring the Islands meet their international obligations; and
- defence.

UK International obligations & the negotiations to join the EU (then EEC)

Prior to 1950, all international agreements signed by the United Kingdom were deemed to apply to the Crown Dependencies, unless otherwise stated. However, in October that year, the Foreign Secretary published a memorandum (the Bevin Memorandum) setting out the "Position of the Channel Islands and Isle of Man in relation to Treaties and International Agreements".

The memorandum explained that: "*His Majesty's Government have come to the conclusion that it would be more consistent with the constitutional position of these Islands to regard them for international purposes as not forming part of the United Kingdom*".

It went on to say that, "*accordingly, any treaty or international agreement to which His Majesty's Government in the United Kingdom may become a party after the date of the present despatch will not be considered as applying to the Channel Islands or the Isle of Man by reason only of the fact that it applies to the United Kingdom of Great Britain and*

Northern Ireland, and any signature, ratification acceptance or accession on behalf of the United Kingdom will not extend to the Islands unless they are expressly included'.

By the time the United Kingdom came to negotiate its accession to the EEC it was clear, therefore, that the Isle of Man would not necessarily be included within the United Kingdom's accession, without wishing to be.

But as it then currently stood, the Treaty of Rome (establishing the EEC) stated that "*Article 227(4) specifically applies the Treaty to all European territories for whose external relations member states are responsible'*. (Kilbrandon)

The Isle of Man and the other Crown Dependencies requested that special terms be negotiated on their behalf. The Treaty was subsequently amended, dis-applying the terms of Article 227(4) to the Crown Dependencies, and setting out the special and limited relationship between the Community and the Islands, the terms of which were attached to the UK's Act of Accession to the Treaty.

The Isle of Man's Relationship with the EU

As noted above, the relationship between the Isle of Man and the EU is set out in Protocol 3 to the UK's Act of Accession by which the UK became a member of the EU, and not within the Treaty (as amended) itself. The Isle of Man's relationship is dependent, therefore, on the UK's continued membership of the EU.

The Protocol allows the Island to be part of the EU customs area which permits the free movement of manufactured goods and agricultural products in trade between the Island and the Union. Apart from the requirements of the Protocol, in particular that the Isle of Man must apply the same treatment to all natural and legal persons of the EU, the other Union rules do not apply. In addition, the Island's relationship with the Union allows it to trade with countries in the European Economic Area similarly to its trade with the Union itself.

The impact of EU legislation and policies on the Island does, however, go beyond the scope of the Protocol, as follows –

- UK agreements/relations – there are several policy areas where, because of bilateral agreements with the UK such as on Customs and Excise/VAT, National Insurance, Health, and certain benefits, EU rules may be applied in order to stay in step with the UK (which itself may be subject to EU obligations in these areas). A prime example is VAT, where the Island is treated *as if* it were part of the EU for VAT purposes.
- Transactional issues – there are many instances where goods produced must meet EU standards if they are to be sold to EU consumers. Journeys begun or ending in the EU are also subject to EU rules and those providing services to customers in the EU may need to meet EU standards or demonstrate effective equivalence.
- Voluntary or reputational issues – the Isle of Man may choose to adopt EU measures and legislation voluntarily – as it has in respect of certain environmental standards – or indeed for reputational reasons, for example, when it adopts EU sanctions measures.

- Global standards – there are several examples where the Isle of Man has adopted global standards which have been agreed or implemented by or in conjunction with the EU.

What would happen to Protocol 3 if the UK left the EU?

If the UK left the EU, then its Act of Accession would cease to have effect, and Protocol 3, which is attached to it, would fall away. This would not happen immediately, however – and the withdrawal process is set out in more detail below.

No Member State has ever left the EU, and so there is no model or template to follow, but the Treaty on European Union envisages at Article 50 that the UK would have two years – from notification of its intention to leave – to negotiate a withdrawal agreement. (The Danish Territory of Greenland, which is a Danish dependency, left the EU in the 1980s, upon achieving greater autonomy/‘home rule’ from the Kingdom of Denmark. It was not a Member as such, and had only a limited relationship with the Community, but even so, this process was long and drawn out).

The withdrawal agreement would need to set out the terms of the UK’s new relationship with the EU, if any, and if the Isle of Man were to wish to maintain some form of relationship with the EU, the withdrawal agreement would also need to include provisions which covered the Island.

In very simple terms, however, as the UK would no longer be a Member State, no matter what happened, the Isle of Man’s relationship with the EU would need to be rebuilt.

The leaving process – Article 50 (from House of Commons Library Paper Number 13/42)

Article 50 of the amended Treaty on European Union (TEU) allows a Member State unilaterally to leave the EU in accordance with its own constitutional requirements.

In the UK this would require an Act of Parliament to repeal the European Communities Act 1972 and to implement any negotiated agreement with the EU on their future relationship.

Similarly, if Protocol 3 ceased to have effect, then the Isle of Man’s European Communities (Isle of Man) Act 1973 would need to be repealed, and replaced with whatever was required to give effect to any new relationship established in its place.

Article 50(2) states that:

A Member State which decides to withdraw shall notify the European Council of its intention. In the light of the guidelines provided by the European Council, the Union shall negotiate and conclude an agreement with that State, setting out the arrangements for its withdrawal, taking account of the framework for its future relationship with the Union. That agreement shall be negotiated in accordance with Article 218(3) of the Treaty on the Functioning of the European Union. It shall be concluded on behalf of the Union by the Council, acting by a qualified majority, after obtaining the consent of the European Parliament.

Article 218(3) specifies:

The Commission, or the High Representative of the Union for Foreign Affairs and Security Policy where the agreement envisaged relates exclusively or principally to the common foreign and security policy, shall submit recommendations to the Council, which shall adopt a decision authorising the opening of negotiations and, depending on the subject of the agreement envisaged, nominating the Union negotiator or the head of the Union's negotiating team.

Sir David Edward, a former judge of the Court of Justice of the European Union, has noted (quoted at p. 10 "Leaving the EU" Research Paper 13/42 1 July 2013 House of Commons Library), a long negotiation period under Article 50 TEU would be necessary because "withdrawal from the Union would involve the unravelling of a highly complex skein of budgetary, legal, political, financial, commercial and personal relationships, liabilities and obligations". The two-year negotiating period would aim to conclude both the withdrawal agreement and any consequent amendments to the EU Treaties.

In March 2016 the UK Cabinet Office published a paper entitled "The process for withdrawing from the European Union"³, in which it concluded that "*It is...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*".

The decision to leave does not need the endorsement or formal agreement of the other Member States. Withdrawal can happen, whether or not there is a withdrawal agreement, two years after the leaving State notifies the European Council of its intention to withdraw. However, the terms of Article 50 TEU imply an orderly, negotiated withdrawal.

During the negotiation, the withdrawing Member State would continue to participate in other EU business as normal, but it would not participate in Council of Ministers or European Council discussions or decisions on its own withdrawal. The withdrawing state would be released from its obligations under the Treaties upon entry into force of the withdrawal agreement, or two years after its notification to the European Council. This period may be extended by unanimous agreement.

An EU-UK Withdrawal Agreement

Without precedent, there is no way of knowing what a withdrawal agreement would look like, but it would need to address three broad themes –

- How will the rights and obligations acquired by UK citizens under EU law either continue or be extinguished?
- What will be the future relationship between the UK and the EU?
- What will the transitional arrangements be (including the UK's role within the institutions and decision making bodies)?

It would not be possible for the UK to withdraw from, for example, the Common Agricultural Policy overnight without causing enormous disruption for farmers. Transitional arrangements

³https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/503908/54538_EU_Series_No2_Accessible.pdf

for an alternative regime to be put in place would have to form part of the withdrawal agreement. Similar problems would have to be dealt with in relation to projects, joint ventures, etc., for example in the field of research, which are being funded by the EU as part of a long-term programme.

In accordance with Article 50(2) TEU, a withdrawal agreement is an international agreement between the EU and a departing Member State. Taking into account the potential comprehensiveness of such an agreement, it may fall across different categories of competence, which are either shared between the EU and its Member States or belong exclusively to the EU. Unless decided otherwise, a withdrawal treaty may have to be concluded as a mixed agreement, making the ratification procedure much longer and more complex as it will involve negotiating with the Member States bilaterally. It has to be emphasised that a departing Member State will be treated as a third country during such negotiations. Moreover, unlike accession treaties, withdrawal agreements do not form part of EU primary law. Unless a special formula is developed, therefore, they cannot amend the treaties on which the EU is based. This implies that, alongside an international treaty regulating withdrawal, the remaining Member States would have to negotiate between themselves a treaty amending the founding EU treaties in order to repeal all provisions touching upon the departing Member State.

Further complexities may be added if a departing Member State chooses to make a rapid move from the EU to the European Economic Area (EEA)⁴ instead. That would necessitate a third treaty regulating the terms of accession to the European Free Trade Association (EFTA) and a fourth to deal with the accession to the EEA. The latter would require the approval of the EU and its Member States, the EFTA-EEA countries and the departing/joining Member State.

Article 50(2) TEU merely provides guidance in that it requires arrangements for “withdrawal, taking account of the framework for its future relationship with the Union”. A comprehensive set of institutional and substantive provisions would certainly be required to turn the political desire to leave the EU into a legal reality. To start with, it would be necessary to delete all provisions and protocols annexed to the founding treaties touching upon the departing Member State. A decision would have to be made as to the cut-off date for the participation of a leaving Member State in the work of all EU institutions, the newly created European External Action Service and the plethora of agencies, organs and advisory bodies. This would have to take place in two stages: phase one should cover the period of withdrawal negotiations; phase two the ratification of a withdrawal agreement. It seems logical that nationals of the departing Member State should be allowed to take part in all the meetings until the formal date of exit. However, the key question is to what extent a leaving Member State should be allowed to shape the legislation it ultimately wishes to withdraw from. Another related issue is the status of EU staff members who hold the nationality of the departing Member State. A number of employment law issues will need to be attended to. Moreover, the status of various EU bodies which have their seat in the departing Member State will have to be considered.

New relationship – the options

⁴ The European Economic Area (EEA) brings together the 28 EU member states and 3 of the EFTA (European Free Trade States- Iceland, Norway and Liechtenstein) and it enables to 3 EFTA states to participate fully in the Single Market including the four freedoms.

The different scenarios for a new relationship between the UK and the EU have been discussed in numerous articles and papers produced by a wide variety of professional bodies, interest groups, and think tanks and are discussed in more detail in Section 10 of this report (many of these are listed in the House of Commons Library publication "The UK and the EU: reform, renegotiation, withdrawal? A reading list" Number 07220)

Broadly speaking, most list similar options. TheCityUK, a high-powered financial and professional services lobby group, commissioned a paper from global law firm Clifford Chance. The April 2014 paper entitled "A legal assessment of the UK's relationship with the EU – a Financial Services Perspective" sets out the following possible routes –

Three scenarios where the UK remains in the EU

1. Reform within the existing treaties. This scenario imagines a UK which does not seek to alter radically the balance of competences between itself and the EU under the threat of departure.
2. "EU – minus". A renegotiated version of the UK's current membership, where the UK secures opt-outs from certain areas while retaining its current rights and obligations in others and/or instigates institutional reforms to repatriate competencies to all Member States.
3. "EU-plus". This scenario examines the possibility of the UK becoming more involved in the EU by giving up its current opt-outs.

Five scenarios where the UK leaves the EU

1. EEA + EFTA membership. The UK would leave the EU and could emulate Norway in becoming a member of the EEA and EFTA.
2. Bilateral Agreements + EFTA. The UK would leave the EU and could emulate Switzerland in agreeing sector-by-sector treaties with the EU and Free Trade Agreements with EFTA countries
3. Customs Union. The UK would leave the EU and could emulate Turkey and enter into a Customs Union with the EU.
4. UK/EU FTA. The UK would be outside the EU but could seek to negotiate a comprehensive Free Trade Agreement with the EU.
5. The WTO option. The UK would be outside the EU and rely on its membership of the World Trade Organization as a basis for trade with the EU.

The UK Prime Minister David Cameron has stated that he would renegotiate the UK's relationship with the EU and then campaign in the referendum for the UK to 'remain' in the EU. He is therefore supporting option '2' (EU-minus). The other options, however, will not be put before the electorate at the referendum, with the choice being either to 'remain' in the EU or 'leave'.

This section, being confined to the legal aspects of the UK's potential breakaway from the EU and the impact on the Isle of Man, focuses on how the Isle of Man might participate in

negotiation of the withdrawal agreement, and how it might be given effect in Manx law. The different options are discussed in more depth in section 10 of this paper.

The Isle of Man's Future Relationship with the EU

The EU Treaties allow only for sovereign states to become members of the EU, as does the Convention establishing the European Free Trade Association. Similarly, the EU can only sign association agreements with sovereign states – such as those currently being negotiated with the so-called 'micro-states' of Andorra, Monaco and San Marino.

It is not possible, therefore, for the Isle of Man to either become a Member of the EU, or to join EFTA and accede to the European Economic Area (EEA) Agreement, or to sign an association agreement with the EU, in its own right.

The Isle of Man's relationship with the EU is, therefore, dependent upon the UK's continued membership of the EU – and the retention of Protocol 3 – or, in the event that the UK chose to leave the EU, on the arrangements negotiated by the UK on its own behalf.

Negotiations

As has been noted, the UK is responsible for the Isle of Man's international relations. Although advances in the Island's international profile have been made in the years since the UK negotiated Protocol 3 on behalf of the Crown Dependencies, these have been confined to two principal areas:

- Firstly, in the negotiation and signature of bilateral agreements under entrustment (so far confined to Tax Information Exchange Agreements and Double Taxation Agreements); and
- Secondly, through the participation in the work of certain international bodies (where their constitutions allow it), and the building of informal relationships with other governments and institutions.

Any negotiation with the EU regarding the Isle of Man's future relationship will fall to the UK to conduct, with the Isle of Man contributing to the negotiations through the UK delegation. It has been suggested by the House of Commons Justice Committee and accepted by the Ministry of Justice that, in certain circumstances, representatives of the Crown Dependencies may appear as part of a UK delegation, and may deal with international bodies direct. This has been the case in respect of Isle of Man officials appearing in the EU Code of Conduct Group, and in certain UN Committees.

What is clear is that the Isle of Man must identify what it would wish to secure from any re-configuration of the UK's relationship with the EU whether, potentially, a Protocol 3 style arrangement, or perhaps an enhancement of that relationship. Thereafter, the Isle of Man will have to work alongside the UK (and probably in collaboration with the Channel Islands) to secure this, as any such arrangements would form part of the UK's withdrawal agreement.

It is difficult to see how a UK withdrawal agreement would provide for the negotiation of a deeper or more extensive relationship between the Isle of Man and the EU than it has at present, and so any UK withdrawal agreement would need to include terms which mirrored

the terms of Protocol 3, should the Isle of Man Government determine that it would wish to retain that relationship.

What is important is that the mechanics of these discussions are understood, and that the Isle of Man Government ensures that the Foreign and Commonwealth Office understands the Island's priorities, and wish to be included in discussions of the new relationship. Engagement in this regard has already been established and is ongoing.

Conclusion

Whilst the position of the UK, following a vote to leave the EU, remains far from clear, the position of the Isle of Man is similarly difficult to predict.

The legal and constitutional position remains relatively clear, however, in that –

- Protocol 3 in its present form would fall away
- The Island's *European Communities (Isle of Man) Act 1973* would need to be repealed, and new legislation drafted to reflect any new relationship
- The Isle of Man's criteria for a new relationship with the EU would be a matter for the Isle of Man to decide
- This would fall to the UK to negotiate, on behalf of the Island, with the EU
- The Isle of Man would contribute to or potentially form a part of the UK negotiating team for this element of the negotiations

5 – Customs duties, VAT and trade with the EU (Single Market)

Under the terms of Protocol 3, the Isle of Man is part of the customs territory of the European Union, and is designated as such in the relevant EU customs Regulations (the Community Customs Code) which is being replaced by the Union Customs Code from 2016. The Common Customs Tariff, levies and other agricultural import measures apply to trade between the Isle of Man and non-member countries and there is free movement of goods in trade between the Isle of Man and the Union as regards industrial and agricultural products.

In addition, by virtue of the 1979 Customs and Excise Agreement with the UK ("the Agreement"), the Isle of Man applies EU rules as they relate to VAT and to those excise duties which are the subject of harmonisation and underpinned by EU legislation – on alcohol, manufactured tobacco products, and mineral oils and other energy products. EU proposals relating to the harmonisation of VAT "and affecting the various excise duties" will, therefore, apply to the Isle of Man.

This means that the Island is effectively a part of not only the customs territory of the EU (which Protocol 3 explicitly provides for) but also its "fiscal territory" (for VAT and excise purposes); with this status being recognised in the relevant VAT and excise Directives which instruct Member States to treat supplies involving the Island as if being to or from the UK.

By contrast, whilst the Channel Islands are part of the customs territory, they are not part of the fiscal territory, meaning that fiscal border barriers remain – even with the UK.

On a technical/practical level, the Island has direct access and input into, the electronic UK Customs Handling of Import Export Freight (CHIEF) system for handling the clearing of goods into the UK/EU as well as other various electronic systems used by the EU and

Member States to track and verify movements of excise goods, verify the identities of VAT-registered businesses, and to prevent and detect fraud involving VAT and/or excise duties.

In addition, the Agreement also permits effective participation in UK-administered systems, processes and mechanisms – such as the VAT Mini One-Stop Shop (MOSS) for businesses making supplies to other Member States for which VAT is or may be due to that other State and the Alcohol Wholesaler Registration Scheme (AWRS) for business wishing to trade in the wholesaling of alcohol.

Indirect taxation can also be affected by general EU law even where the tax itself is not governed by one of the EU Directives having direct effect in the Island. For example, state aid rules mean that differential rates of air passenger duty for flights to different airports in the UK (so as to effectively subsidise one route, but not others) may be ruled out. Where taxation impinges on “cross-border” supplies, even if this only involves the trade with the UK, complications due to EU competition and equal treatment rules can arise.

Single Market: Free Movement of Goods and Customs Union

As a member of the European Union Customs Union (EUCU), the Isle of Man is considered part of the Single Market as far as the free movement of goods is concerned. Trade between the Isle of Man and the EU is considered intra-EU trade. Furthermore, any trade the Isle of Man conducts with non-EU countries is subject to the Common Customs Tariff and hence any import charges that all external countries must pay to import into the EU (although any such import duties due in the Island are not in fact remitted to the EU). Involvement in the EUCU has other, indirect benefits. For example, the Island has been able to make use of mutual assistance agreements between the EU and third countries in customs matters to provide information and assistance, and so bolster its reputation as a responsible and transparent trading partner.

Although in many ways the Isle of Man is integrated into the Single Market, large elements of EU legislation do not directly apply under the terms of Protocol 3. However, the Island does choose to implement EU rules in many areas to ensure ready access to the Single Market, and to ensure that the Island is not used or perceived as a “back door” to avoid controls and requirements applying to imports into, or exports from, the UK/EU (thus again maintaining the Island’s reputation as a responsible trading partner. The EU is the largest free trade area in the world, and there is, therefore, pressure on businesses outside of the regulated area to voluntarily conform in order to do business within it. In this respect, and regardless of the legal relationship between the Island and the Single Market (i.e. whether the UK remains a Member State or not), there is great pressure to voluntarily conform to many of its regulations in the interests of promoting trade and business.

Increasingly, standards applying to cross-border trade and services are being harmonised. For example, the international trade in goods is being affected by 3 main themes –

1. Increasing use of electronic and online systems for control, e-documentation etc. (such as electronic air waybills), with the new Union Customs Code from 2016 making electronic communications the default between customs authorities and businesses;
2. The requirement for traders to be pre-authorised (such as under the Authorised Economic Operator (AEO) Scheme being introduced in the EU and corresponding arrangements, such as C-TPAT in the USA and MCME in China). This facilitates trade

via the relaxation of clearance procedures (with non-authorised traders bearing greater burdens in terms of time and cost);

3. The requirement for cross-border cargo movements to be subject to security and safety requirements, such as pre-scanning of all containers (and the certified pre-weighing of all export containers), as well as all mail and other cargo sent by air. The AEO-type requirements mentioned above can or will include security control aspects.

Having to meet EU customs standards means the Isle of Man currently has to meet the highest international standards and has, via HMRC and the UK Border Force, links into the systems necessary.

The new Union Customs Code, which comes into operation during 2016, and is being phased in over the following 4 years, includes many provisions directly relating to the 3 themes above – effectively making those themes pre-requisite requirements for international trade.

Possible effects of a UK exit

If the UK left the EU and the Agreement with the UK was retained, providing for goods traded between the Isle of Man and the UK to continue to be liable to the same rates of customs duty, there would continue to be free trade between the Island and the UK.

However, because UK and Isle of Man legislation as it relates to customs matters and VAT is currently based upon EU rules (and, in fact, for the most part customs legislation comprises EU Regulations having direct effect in domestic law), this link would be broken and new rules and rates would need to be established and quantified. These rules, in particular as they relate to external tariffs, would need to be compliant with World Trade Organisation principles (and also, if trade with the EU were to be maintained, compliant with all the requirements of the EU).

In addition, Isle of Man companies trading with the EU would then be subject to external tariffs, as goods coming from the Isle of Man would be classed as imports from a third country (subject to any transitional period that may be negotiated between the UK and EU).

Furthermore, goods exported from the Island to other countries around the world would not, then, be treated as being from the EU, and may also incur additional costs or other barriers, as the EU has negotiated a number of preferential trade agreements with third countries. The UK is likely to have to agree replacement trade treaties with a great number of countries and trade blocs, to replace those to which is party as a Member State, and it would be essential for the interests of the Isle of Man to be taken into account in such negotiations.

There can be no doubt therefore that UK exit from the EU would make producing and exporting goods to the EU and the rest of the world more difficult, and potentially more costly. It could also be the case that imports from outside the EU may become more costly.

Other considerations include but may not be limited to:

- business that continued to trade with the EU would suffer increased administration, compliance and cash flow costs as they would need to separately register and file

indirect tax returns and customs declarations in both territories as trade with the EU would become imports and exports;

- residents would be faced with customs/tax barriers when they travelled to the EU and the possibility of double taxation on their purchases;
- residents would be restricted to customs limits on excise goods of 1 litre of spirits and 200 cigarettes (the old "duty-free limits" that continue to apply to travel involving non-EU territories). Thus any resident buying alcohol or tobacco on their holiday to the EU would either have to pay additional duty and VAT on the excess or forfeit the goods on return to the Island.
- residents would be subject to further checks to ensure that the Isle of Man Treasury was receiving all the VAT and duty it was due on purchases made in the EU. For example, online or mail order purchases or downloads via the Internet. Such checks would include all postal packages from the EU being examined and vehicles being examined as they arrived back on the Island, no doubt leading to delays and potential disruption.

Economic Impact – Government Revenue

Whilst the potential effects on the export-led sectors of the economy are discussed in more detail in section 6 below, the effect of the UK leaving the EU on Isle of Man Government revenues may be significant, potentially reducing trade and affecting employment and local consumption/spending, in turn reducing Government revenue. To place this into some context, during 2014/15, the value of trade in goods and services between businesses registered for VAT in the Isle of Man and businesses in the EU, excluding the UK, exceeded £300 million.

The majority of Isle of Man Government revenue derives from indirect taxation, which is generated by levies on imports and excise duties on particular goods, but mostly from VAT, whether collected in the UK or the Isle of Man, and relating to goods consumed or services used and enjoyed in the Isle of Man (shared according to the VAT sharing arrangements).

The EU, and its centrepiece, the Single Market, were created essentially to facilitate free trade, and hence increase the volume of trade. Withdrawal from it, would therefore be likely to make trade more difficult, and potentially make Isle of Man goods and services more expensive for customers within the EU, and so reduce the overall volume of exports.

The ability to collect information and participate in EU-wide systems may be curtailed, which may impact in other areas, including potential reputational issues. In addition, it is assumed that the UK would continue to follow EU trade and financial sanctions measures – as these generally implement UN requirements. For reputational and practical purposes, it can also be assumed that the Isle of Man would continue to keep in step with the UK in this area, and therefore match prevailing international standards.

One of three key aims of the Isle of Man Government is to diversify the economy, and although relatively small, the production of high-value manufactured products, as well as locally grown agricultural produce, are important sectors of the economy. Furthermore, the ownership and control of valuable assets (properties, ships & yachts and aircraft) may also be impacted by changes in customs and VAT rules. Yachts and aircraft, for example, would no longer qualify as having EU status, and would become liable to be treated for VAT and customs purposes like those from other third countries, with potentially heavy administration and tax liabilities. Whilst the gambling industry in the EU is not currently a part of a harmonised Single Market, there is increasing cross-border and multilateral co-operation of

this sector too, and if wholly outside the EU any possibility of the Island's e-gambling sector being able to secure favourable treatment would be far less likely.

Furthermore, if the UK was no longer subject to EU VAT rules, it may seek to reduce the rates or level of VAT levied, which the Isle of Man would be obliged to match adhere to – because of the Agreement – and so would see further reductions in Government revenue.

Conclusion & recommendations

There can at this stage be no clear picture of how trade might be affected by the UK withdrawing from the EU, but reduced access to the Single Market and increased costs would undoubtedly reduce the overall level of trade which, in the context of the Island, may be exacerbated by any trader migration from the Island as a result of UK withdrawal. This is likely to reduce the levels of revenue derived from indirect taxation.

Key areas for the Isle of Man will be –

- to seek continued customs union with the UK, and continuation of the Agreement;
- to ensure that any trade agreement/customs union that the UK seeks with the EU is extended to include the Island; and
- that any trade agreements between the UK and third countries should take account of the Island.

6 – Nationality, population & the free movement of people

Isle of Man resident population

The Isle of Man's resident population according to the 2011 census was 84,497 comprising: 78,750 (93.2%) British nationals; 3,609 (4.3%) nationals of other EU Member States; 310 (0.4%) nationals of other European countries and 1,828 (2.1%) nationals from the rest of the world.

Based on this data, the vast majority of people living in the Isle of Man are British Citizens. The 2011 census showed that 48.1% of the population were born in the Isle of Man, 35.9% in England, 1.1% in Wales, 3.2% in Scotland, 2.0% in Northern Ireland and 0.2% in the Channel Islands. This suggests that of the 93.2% of the population which is British, 90.5% of the population is British born, with the remaining 2.7% deriving their British nationality in other ways. British citizenship can be obtained by naturalisation or registration under the British Nationality Act 1981 which extends to the Isle of Man.

Article 3 of Protocol 3 states that "*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 Community provisions relating to the free movement of persons and services.*"

The Protocol goes on to identify 'Manxmen' at Article 6 as "*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 a grandparent was born, adopted, 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." (NB the term 'Manxmen' includes women).

The 2011 census identified those who were born in the Isle of Man, and further identified, of those who were born in the Isle of Man, how many of them did not have a UK born parent or grandparent. Putting aside those who may have lived in the UK for more than the required five years, the 2011 census identified 12,781 Manxmen (with a further 455 people born in the Isle of Man who did not answer the question concerning the birthplace of their parents and grandparents).

Those defined as 'Manxmen' have a stamp placed in their passport stating that "*holder is not entitled to benefit from European Community Provisions relating to employment or establishment*". This means that whilst permitted to live and work in the UK (under UK law), their rights to do so in other EU Member States may be restricted, although in practice, 'Manxmen' may be treated in the same manner as other UK citizens.

Provisions relating to the free movement of persons are discussed below, but for the purpose of this discussion, it is worth noting that the impact of a vote by the UK to leave the EU may affect people currently living in the Isle of Man in different ways depending upon whether they fall into the classification of 'Manxmen', British Citizens (who are not 'Manxmen'), citizens of other EU Member States, and the rest (non-EEA Nationals, and those from the rest of the world).

Free movement of persons within the EU

The free movement of persons is one of the four 'fundamental freedoms' underpinning what is known as the EU's Single Market, an area without internal frontiers designed to ensure the free movement of persons, goods, services and capital. The European Economic Area (EEA) combines the 28 EU member states and 3 of the EFTA (European Free Trade Association) States - Iceland, Norway and Liechtenstein, and it enables the 3 EFTA states to participate fully in the Single Market. Switzerland is not a member of the EEA (but is a member of EFTA) and its position in relation to free movement of persons is complex.

The rules governing the right to free movement distinguishes between nationals from EEA Member States and the rules applicable to those from outside the EEA – who are known as 'third country nationals'. In the UK, third country nationals are further divided into categories of 'visa' or 'non-visa' nationals.

Free movement of people in the EU was originally centred on those who were economically active, and designed to facilitate the free movement of workers, self-employed persons and those providing services in order to support the creation of a free market for labour. Changes in EU legislation and its subsequent interpretation by the European Court of Justice (ECJ) means it has developed from a purely economic concept to a social concept. In the late 1960s, two key measures implemented the rights of free movement for workers: Directive 68/360 on free movement for workers within the then European Community (EC); and Regulation 1612/68 on the abolition of restrictions on movement and residence within the EC for workers of Member States and their families.

This was further developed in 1990 when the EC adopted three Directives which conferred a general right of movement and residence on retired people, students and people with

independent means, provided that they had sufficient resources and medical insurance. This reflected the gradual change which had been taking place in relation to the link between economic activity and free movement – moving towards the idea of migrants as individuals with rights in their host Member State.

The Maastricht Treaty (The Treaty on European Union) explicitly introduced the concept of Union citizenship into the EC Treaty in 1992, together with a number of associated rights. This included the right to move and reside freely in Member States subject to limitations and conditions laid down in the Treaties and in EU secondary legislation. It created the European Union and formalised the recognition of the status of 'citizen of the Union', with the associated rights and duties, for every national of a Member State. The case of *Baumbast* ^[1] effectively confirmed the severance of the absolute link between migration and the need to be economically active.

The earlier legislation was replaced in 2006 by Directive 2004/38/EC (known as the 'Free Movement Directive'); and Regulation 1612/68 by Regulation 492/2011 (the 'Free Movement of Workers Regulation'). Since the adoption of the 2004 Directive the ECJ has continued to clarify and, in some cases, expand free movement rights through various rulings such as the *Metock* judgement (2008) on free movement rights for family members.

Third country nationals are also able to derive rights, regardless of their own nationality, if they are the family members of an EU citizen who is living in another EU member state and exercising their treaty rights in that member state. Such derivative rights grants non EEA nationals a right to family reunification in a host country which prevails over that country's domestic immigration restrictions. The primary derivative rights cases in the UK are *Surinder Singh* ^[2] (1992) which permits non EU spouses of EU citizens to reside in a Member State by virtue of exercising their treaty rights (which circumvents any domestic immigration law restrictions) and *Zambrano* (2011) ^[3] which extends derivative EU rights of free movement to wider family members and carers of EU citizens.

The Isle of Man & free movement of persons

Treaty provisions, subsequent Directives and European case law in this area fall outside of the scope of Protocol 3 and do not extend to the Isle of Man. However, Article 4 of Protocol 3 states that "*The authorities of these territories shall apply the same treatment to all natural and legal persons of the Community*" which means that, in relation to the free movement of people, rights afforded to British Citizens coming to the Isle of Man from the UK must be applied equally to citizens from all Member States. Therefore, because all British Citizens have the right to live in the Isle of Man, it follows that citizens from all EU Member States also have the right to live in the Isle of Man. In practice this means the Isle of Man can impose barriers to the free movement of EU citizens such as the work permit legislation or restrictions upon whom may obtain social security benefits or housing rights within its domestic law. However, any such restrictions must be applied equally to all EU citizens and therefore, for example, the Isle of Man cannot distinguish between British or Irish citizens and other EU citizens when it applies work permit legislation.

^[1] <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A61999CJ0413>

^[2] <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A61990CJ0370>

^[3] <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A62009CJ0034>

British and Irish Citizens may travel freely within what is known as the Common Travel Area (being the United Kingdom, Republic of Ireland, the Isle of Man and the Channel Islands)(CTA). The principles of the CTA, as set out in the United Kingdom's Immigration Act 1971, mean that travelling within the CTA is treated as a local journey and certain people are not subject to controls on such journeys. Additionally, a person without a right of abode within the CTA but has been given permission to enter and remain within one of the CTA territories (i.e. a third country national with a valid visa) is also not subject to control on journeys within the CTA and is free to enter any other part of the CTA. This position is modified slightly for third country nationals who enter the CTA from the Republic of Ireland. A third country national who enters the Isle of Man from outside the CTA, whether by private jet, yacht, cruise ship or direct charter flights would be required to pass through immigration control. The future existence and operation of the CTA between the UK and Ireland would be a highly political issue if the UK were to leave the EU but the Isle of Man (and the other Crown Dependencies) would legitimately expect to be a part of any future re-negotiation of the current arrangements. There are political and historical factors which would suggest that the current CTA arrangements would remain in place but this cannot be guaranteed.

The right to enter and remain in the UK is governed by various immigration acts and certain of these Acts of Parliament have been extended with modification to the Isle of Man. Under the Immigration Act 1971 the UK Secretary of State has the power to make immigration rules which set out the conditions under which migrants may apply for visas and which govern the conditions of leave to enter and remain. In the Isle of Man the Council of Ministers has the power to make immigration rules under the Immigration Act 1971 as it applies in the Island. The Isle of Man immigration rules are similar but not necessarily identical to the UK immigration rules. In applying the Isle of Man rules, the Isle of Man immigration service relies upon the UK guidance so far as it is applicable.

Certain domestic legislation such as the Control of Employment Act 2014 creates restrictions on persons who are either not Isle of Man workers or who have lived in the Isle of Man for certain periods. These restrictions govern access to employment without requiring a work permit, and eligibility for government services and benefits and access to public sector housing, although as noted above, these restrictions must not cut across equal treatment provisions as set out in Article 4 of Protocol 3

British Citizenship

British nationality is acquired under the British Nationality Act 1981 which extends automatically to the Isle of Man under section 53 of that Act. EEA nationals and non EEA nationals can apply for British nationality if they meet certain requirements including residency in the Isle of Man for specified period prior to application. Persons who are naturalised as a British Citizen in the Isle of Man and who apply for the British Passport receive the "Manxman" stamp in their passports.

What if the UK was to leave the EU?

It is difficult to state what the exact impact of the UK voting to leave the EU would be on Isle of Man residents as this very much depends upon the terms of the new relationship between the UK. Whilst the actual effects of Brexit in relation to free movement cannot be accurately predicted, clearly one factor would be an individual's current status under Isle of Man, UK and EU law.

It is important to remember that any changes would not be instantaneous. If the UK referendum voted for Britain to leave the EU, then the UK Government would have two

years to negotiate a withdrawal agreement under Article 50 of the EU Treaty. It would take additional time for negotiations and entry into replacement treaties or agreements governing new arrangements or relationships between the EU and the UK. Such new relationships could either be between the UK and the EU as a whole or bilateral agreements between the UK and individual member states. It is the usual practice of the UK Government to consult with its Crown Dependencies before it enters into arrangements with third parties which would have an impact on them and it is expected that dialogue and consultation would occur in these circumstances.

Following withdrawal from the EU, the UK would recover its ability to restrict immigration from EU member states in the same way as it exercises controls on immigration from the rest of the world. As the Isle of Man's immigration legislation is intrinsically bound with that of the UK, the Isle of Man Government would be likely to decide to follow suit in order to preserve the current CTA arrangements. The UK's exit would permit a range of immigration policies to be considered.

One possible policy is for the UK to decide that it is in the UK's economic interest to allow free immigration from the EU to continue. This would maintain an inflow of labour to replace the retiring baby boomer generation and to fill new jobs where there is a deficit in British workers – either because of skills shortages in the domestic workforce or lack of inclination to do specific types of low-paid work. However, the UK would be able to place restrictions on such migrants' access to benefits and housing in a similar manner to the current Isle of Man position. Arguably, the UK Government would lack a political mandate for this policy if the British electorate have voted for Brexit on the basis that the UK should be allowed to control its own borders. If the UK adopted a Switzerland model, an association agreement with free movement, then this would involve little actual change to the status quo. However, if Britain joined the EEA it would have to agree to free movement of people in order to have full access to the Single Market as the other members of the EEA do. This model perhaps less likely as it does not address UK political problems with the EU migration.

Alternatively, the most radical policy would be the imposition of entry requirements on new EU migrants and/or to "expel" existing EU migrants. Under this policy, EU nationals may be incorporated into the current immigration system for third country nationals. This would require EU migrants to apply for visas under the Point Based System ("PBS") and meet the other immigration requirements. This would severely restrict the ability of low-skilled European migrants to work in the UK as the PBS only permits skilled migrants with a job offer with a salary of £20,880 (current figure) to apply for visas. The impact on students is even more uncertain but there may be impacts for any Isle of Man students who wish to participate in the ERASMUS scheme or attend European universities.

If EU migration for work and/or study was amalgamated into the current immigration framework then the UK government would probably have to relax certain rules to ensure that shortages in certain low-skilled occupations such as seasonal farm work could be met. It might also consider implementing separate rules and/or quotas for EU nationals. It is probably also important to be aware that many EU migrants may attempt to "get in before the door shuts". This may lead to an increase in applications for British Citizenship or increased numbers of EU job seekers.

Upon exit it would seem logical to permit existing EU migrants in Britain to remain and there is a legal basis for this contained in the Vienna Convention on the Law of Treaties 1969 and in relation to Greenland's exit from the EEC. This would also permit British citizens currently

living elsewhere in the EU, whether as workers or retirees, to enjoy reciprocal rights and remain living abroad.

However, the future right of EU citizens to live and work in the UK may be restricted, and presumably, the right of British Citizens to live and work in the EU would similarly be restricted.

Immigration, and in particular, the British Government's wish to restrict access for migrants to certain benefits, has been one of the key areas in the renegotiation process, and is likely to be one of the key features of the referendum debate. It is unlikely, therefore, that if there was a vote to leave the EU, that free movement provisions would be replicated in their current form in any new settlement which the UK negotiated.

For Isle of Man residents, the only certainty at this stage is that if the UK votes to leave the EU, and then places restrictions upon EU citizens to either come to the UK, or indeed to remain there, there would most likely be pressure to replicate such restrictions in respect of the Isle of Man. If the Isle of Man wishes to maintain the current CTA arrangements and, given that the UK has ultimate responsibility for the Isle of Man's international relationships, then the Isle of Man Government may have little choice but to replicate these restrictions.

From the figures available, around 3500 EU nationals live in the Isle of Man and potentially the ability for these people to remain in the Isle of Man could be brought into question. It should be noted that other factors such as them acquiring British Nationality, having a British spouse or children or the UK's obligations under the Vienna Convention may be a factor.

It is not known how many people from the Isle of Man currently live and work in the EU, but estimates are that there are 2 million British Citizens doing so, and it must be assumed that their right to continue doing so may be affected, should the UK determine to leave the EU, unless grandfathering rights can be negotiated for such citizens. The ability of those Isle of Man residents who are British Citizens and "non-Manxmen" to exercise rights of free movement in the EU in future is likely to be restricted. Manxmen do not currently enjoy rights of free movement in the EU and therefore they would not experience any change to the current arrangements.

On a separate but related point, it is reasonable to assume that the future requirements for holders of British Passports travelling to EU countries (such as a requirement to obtain a visa, passport compatibility, border checks etc.) would apply equally to holders of Manx variant British Passports. Any such arrangements would, most likely, be applied equally irrespective of whether that person's passport contained the "Manxman" stamp but again this cannot be said with certainty and would depend upon the terms negotiated by the UK with the EU.

Important considerations for the Isle of Man

The impact on the Island of these potential changes can be set out as follows –

- the ability of non-British EU citizens to live and work in the UK and Isle of Man could be restricted, and this may well impact upon the ability of Isle of Man industries to source labour. The work permit system and existing restrictions to benefits already provides the Isle of Man with enough flexibility to regulate and control its population adequately.

- the working of Common Travel Area may be impacted and it could be that the free movement of people between the UK (and Ireland, the Isle of Man and Channel Islands) could be affected
- British Passports issued in the Isle of Man would no longer be required to comply with the EU standard, which may mean changes to the technology used and its associated cost implications, along with the possibility that existing passports may be required to be replaced/exchanged for new ones. Even if the UK opted to leave the EU it may wish to retain harmonisation on matters such as EU standards for passports in order that its citizens can travel freely, subject to the EU agreeing to this. The IOM has very little discretion in relation to the standards applied to Island variant passports which are British Passports issued in the Isle of Man, Channel Islands and Gibraltar.
- Many British Citizens originally from the Isle of Man who now live and work in the EU may find that their ability to continue to so is curtailed and or restricted or subject to conditions but this may also depend upon the length of time they have spent in the relevant country as they may have obtained rights to remain in that country.

7 – Economic Impact

Overview

Amongst the many reports/assessments which have been published in the last 18 months as to what the economic impact of UK withdrawal from the EU might be, there is no clear consensus. Similarly, therefore, this cannot be determined for the Isle of Man.

The Isle of Man has a diverse, successful economy containing firms which are amongst the very best in the world in their respective sectors.

To understand the nature of the inter-dependencies between the various sectors of the Isle of Man economy and the UK's status as an EU member – which includes the current Protocol 3 relationship between the Isle of Man and the EU – this section gives an overview of each of the main sectors of the economy, and considers how each might be affected by 'Brexit'.

7.a – Financial Services

When the UK joined the EU and Protocol 3 was negotiated, the Island's financial services sector was not of the size and status that it is currently. Consequently, services were not included within the Island's trading arrangements with the EU.

In 2013/2014 the financial services sector in the Isle of Man generated 37.8% of the Island's National Income, with 15% coming from Insurance, 8% from Banking, 10% from other finance and business services and 3% from trust and Corporate Service Providers.

Given that the Isle of Man's financial services industry has not (apart from special arrangements with the UK) enjoyed free access to the EU over this period, much of its overseas growth has arisen from servicing other markets such as the Middle East and Asia.

There are three ways in which the Isle of Man financial services industry has been indirectly influenced by the EU, as a result of the UK's membership:

- Through the Island's close relationship with the City of London and the broader UK economy, which may be adversely affected should the UK leave the EU.
- Through the relationship between the UK and Isle of Man regulators and membership of the EU supervisory colleges.
- Through issues which may affect access to the EU market (third country equivalence) and access to the UK and wider EU market.

Banking and Wealth Management

Banks and other financial institutions in the Island provide services to local and international personal customers, corporate and business clients (direct and introduced) and people holding funds on behalf of others.

A wide range of products and services are provided including savings, current accounts, private and premier banking, investments, lending, treasury services and foreign currency accounts. A simple breakdown of the assets and liabilities held by banks in the Isle of Man is shown in **appendix 1**, separately identifying UK, and other EU flows. Further, the Isle of

Man Financial Services Authority publishes a quarterly statistical bulletin on its website, which also includes the information in **appendix 2**.

The banking sector in the Isle of Man is fully regulated and supervised on both a prudential and conduct basis. Banks in the Island are also generally subject to wider group consolidated supervision and need to take into account not only local legislation in devising policies and procedures, but also that of their wider groups, which are mainly in jurisdictions considered to be equivalent, for both prudential and other purposes (including, for example AML/CFT and for Data Protection purposes).

An example of where the Isle of Man has voluntarily adopted certain EU measures in order to maintain the right to conduct cross border transactions is that of SEPA (the Single Euro Payments Area) whereby the Isle of Man has had to adopt certain legislative measures in order that Isle of Man banks can conduct more cost effective cross border Euro payments.

Funds management and administration

The Isle of Man had \$21.37bn Net Asset Value under management⁵ as of September 2015 and a full complement of supporting professional services including fund administrators, legal firms, fiduciaries and custodians. It excels in specialist asset classes and prides itself on customer responsiveness and scalable solutions from small syndicates to capital market listings of investment vehicles.

The fund management sector forms a small part of the Isle of Man's financial services sector overall. Clients include both local and international persons, using the services of businesses such as financial advisors, stockbrokers and discretionary portfolio managers. Non-retail funds represent the most significant elements of the collective investment schemes / alternative funds sector. Overseas funds (those incorporated overseas but administered in the Isle of Man) represent the element of the sector that has seen the most significant positive growth in recent times.

In the funds industry, decisions affecting the location of business within this sector have arguably been the most affected by EU market access in the past and such businesses have therefore tended to gravitate towards Ireland and Luxembourg in order to be within both single market and single currency while those in the Isle of Man have had to look to serve markets elsewhere.

By comparison, the financial services sectors of both Jersey and Guernsey, including funds, are in a similar position to those in the Isle of Man concerning issues around EU access and thus have tended to look for other markets such as the Middle East and Asia. However, the funds industries in those islands are somewhat bigger than the Isle of Man, partly because they have chosen not to be within the VAT arrangements and therefore do not have to apply VAT charges on certain services (e.g. management fees) provided to funds

Insurance and Pensions

Insurance is the largest of the Isle of Man's financial sectors in terms of contributor to GDP (15%) and also a major employer with over 2,000 workers and some of the life insurance companies employing several hundred staff each.

⁵ <https://www.gov.im/lib/docs/iomfsa/statsbulletinsept2015.pdf>

Those life assurance companies present in the Isle of Man are predominately subsidiaries of large internationally active groups headquartered within Europe, mainly the UK. There are a small number of independently owned life insurers on the Island, and one Isle of Man headquartered listed group, the main entity of which is an Isle of Man life assurance company. The sector is well defined and employs the majority of persons employed within the insurance sector.

The non-life sector consists of: insurers of plc groups; insurers of mutual; insurers of private groups; producer owned reinsurers; and not for profit organisations as well as domestic insurers. General insurance business is generally sourced through brokers and in the case of captives, large risk management companies.

A number of the insurance companies are UK or EU parented and despite not having had direct access to the EU market have had to respond to EU Directive Solvency II in order to stay within group capital and risk policy.

Total insurance funds managed by the sector as at 31 December 2014 were £63.9 bn comprising £58.0bn life assets and £5.9bn within captive insurance.

The pensions sector consists of a number of locally based registered schemes administrators which includes a number of the big insurance companies as well as small boutiques. This sector is expanding with funds under management increasing from £1.7bn in 2010 to £7bn in 2014⁶. The majority of this growth is attributable to international pensions and large international occupational schemes sourced predominately from outside of Europe.

Trust and Company Service Providers (“TCSPs”)

The TCSP industry on the Island is large, directly employing over 1200 people. Firms range in size from international businesses with in excess of 100 employees, to small businesses which are in common ownership with the practices of accountants or advocates and often service a similar underlying client base. The industry provides services to some 30,000 client companies of which approximately half are incorporated on the Island and half elsewhere, and to some 20,000 trusts. Most of the business is international in nature. The IOMFSA does not currently collect statistics on origin of business, but estimates indicate that some 40% is from the Isle of Man and the UK, 20% from the rest of the EU and about 40% from the rest of the world. This sector is increasingly involved in business incubation and servicing of trading companies which in part depend on rights of EU access for goods and inclusion with the customs union.

Many TCSP's on the Island are involved in the provision of VAT planning services to both the Super-Yacht & Corporate Jet sectors, with a particular emphasis on their European markets. This has proven a successful endeavor and is partly responsible for the circa 180 jobs on Island servicing those sectors.

The ability to provide VAT planning services to the EU market could be seriously affected by a 'Brexit' depending on any changes in the status of the VAT agreement between the UK and EU and the subsequent indirect effect on the Isle of Man.

⁶ <http://www.iomfsa.im/lib/docs/iomfsa/2015ipaannualreport.pdf> Page 22

Overview of Isle of Man financial services regulation

The Isle of Man Financial Services Authority (IOMFSA) was established in 2015, as a result of a merger between the Financial Supervision Commission ("FSC") and the Insurance and Pensions Authority ("IPA"). It is a statutory board of Tynwald.

The IOMFSA is the regulatory authority for most financial institutions on the Island (money lenders are registered with the Office of fair Trading). It also authorises and supervises Trust Service Providers and Corporate Service Providers as if they are financial institutions. Further to this, the IOMFSA registers and oversees the compliance with AML/CFT legislation for designated businesses and professions (except for casinos which are subject to regulation by the Gambling Supervision Commission).

The IOMFSA's regulatory objectives are –

- (a) securing an appropriate degree of protection for policyholders, members of retirement benefits schemes and the customers of persons carrying on a regulated activity;
- (b) the reduction of financial crime; and
- (c) the maintenance of confidence in the Island's financial services, insurance and pensions industries through effective regulation, thereby supporting the Island's economy and its development as an international financial centre.

The supervision of entities regulated or overseen by the IOMFSA is undertaken through a combination of off-site reviews and analysis and on-site inspection visits.

In order to assist entities with demonstrating their compliance with AML/CFT legislation the IOMFSA also publishes guidance in the form of the Handbook for entities regulated under the FSA208 and the Collective Investments Schemes Act 2008 which in turn is supplemented by sector specific guidance. In addition, the Insurance (Anti-Money Laundering) Regulations 2008 set out additional requirements binding on Insurers with guidance in the form of 'binding guidance' (assessed as other enforceable means as defined by FATF) applicable to insurers writing long term business.

EU competence in relation to financial services

Until the financial and euro area crises, the focus of EU policy-making in financial services focused on improving the Single Market. The focus of global standard setters was on issues of market integrity and the safety and soundness of individual firms and market infrastructure providers, and on protection against financial crime and terrorist financing. Both EU policy-makers and global standard setters viewed issues of consumer protection as ones largely for national authorities and predominantly relevant in the EU to the extent that consumers needed to be protected against the risks related to 'branching', when a firm sets up a branch or provides services remotely.

The EU's single market in financial services, therefore, developed within a wider global framework of international standards that focused on the safety and soundness of financial institutions and the protection against financial crime.

During the period from 2009-2014 the European Commission undertook a raft of regulatory and supervisory reforms, which included –

- creation of the European System of Financial Supervisors, which included the European Banking Authority (EBA), the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA)
- Establishment of the Banking Union, including the Single Supervisory Mechanism (SSM) and Single Resolution Mechanism (SRM)
- Measures to support a more resilient and stable financial system, including an enhanced deposit guarantee scheme (DGS), a new Capital Requirements Regulation and Directive (CRD IV package), a Directive for Bank Recovery and Resolution (BRRD)
- Measures to improve the functioning of financial markets and the stability of financial markets infrastructures, including revised Markets in Financial Instruments Directive and Regulation (MiFID II and MIFIR), the European Market Infrastructure Regulation (EMIR) and the Regulation on Central Securities Depositories (CSDR)
- Measures to reduce the systemic risk stemming from outside the regular banking system, including the Alternative Investment Fund Managers Directive (AIFMD) and the Regulation on Money Market Funds
- Reinforcement of the insurance sector by a risk-based regulatory framework (Solvency II)
- Measures to identify and prevent market abuse, including the Market Abuse Regulation and Directive on Criminal Sanctions for Market Abuse (MAR/CSMAD) and the Regulation on Financial Benchmarks

The current European Commission which took up office in 2014 has focused its attention on the delivery of growth and jobs, with measures to liberalise capital markets and increase access to alternative (to banks) sourced funding at the top of the agenda.

Impact of EU withdrawal on the UK financial services industry – potential indirect impact on the Isle of Man

There is no clear consensus amongst representatives of the financial services industry in the UK as to the effects of a potential UK exit from the EU on the industry. Whilst many suggest that the City could continue to thrive outside the EU, it would appear that most would prefer to see the EU reformed, and for the UK to remain within it.

Some of the Prime Minister's proposed EU reforms aim to protect the City, in order to ensure that non-Eurozone economies are not discriminated against in EU policy making (sometimes referred to as 'caucusing'). This will go some way to ensure that the City – within the EU – retains its status as Europe's pre-eminent financial centre.

The Isle of Man's close ties to the City mean that its performance, and the performance of the UK economy as a whole, has direct impact on the Island's economy and financial services in particular.

Regulatory issues

The Island's regulator is operationally independent and responsible for the regulation and oversight of providers of financial services based on the Island. The Isle of Man's relationship with the UK regulators is one of partnership.

Whilst the regulatory framework adopted in the UK can be persuasive, and this currently incorporates EU provisions, the Isle of Man adopts its own regulatory regime, using UK (EU)

and broader international regimes for comparison as relevant, in order to meet international standards.

The Island does not 'import' UK/EU regulatory regimes per se. For example, the UK/EU does not regulate TCSP activity but regulates mortgage advice, and the Island's regime does the opposite. The banking regime is based upon Basel standards, but matters such as recovery and resolution are linked to UK provisions. For collective investment schemes, the Authorised Collective Investment Scheme is based on the EU UCITS regime (but this does not bring with it recognition in the EU, in fact the Authorised Scheme is still considered a third country Alternative Investment Fund by the EU). The Island's definition of payment services, on the other hand, is based on the EU Payment Services Directive. This is not in order to obtain any EU equivalence, but was deemed important so as to avoid businesses from the EU seeking to relocate to the Island to avoid regulation.

International Standard Setting Bodies (FSB, Basel Committee on Banking Standards, the International Organisation of Securities Commissions, and the International Association of Insurance Supervisors) set the tone and direction for global regulatory framework, and the Isle of Man aims to meet these standards, being subject to inspection and assessment by global assessment bodies, including MONEYVAL⁷.

If the UK were to leave the EU, it would be the case that EU regulations would cease to apply to it and legislation which gave effect to EU Directives could be repealed or amended. But this would not of course mean that the UK would merely abandon its commitments and current regulatory framework, firstly, because much of what the EU has introduced is to set out international standards within the Single Market, and secondly, because adherence to these standards can often allow for market access for third countries (see below).

As with the effects on the economy, it is not helpful to speculate as to how the UK's regulatory framework could alter, and by extension, how that in turn may affect the Isle of Man. What might be inferred, however, is that the UK could find itself in a similar position to the Isle of Man, where it is able to choose how it regulates both to meet international standards, and also, potentially, to choose where it would wish to be deemed 'equivalent' to EU standards.

Market access and third country equivalence

The Isle of Man is part of the Sterling Zone and the UK's payment and clearing system, although it has its own independent regulator and regulatory systems. The Island is a third country for the purposes of EU financial services legislation with the UK responsible for its external relations.

In the past, Member States have largely determined how to permit Third Countries' firms access to their markets, but the EU is increasingly moving into the 'shared competence' area of trade and investment relations with Third Countries.

In providing evidence to the UK's own Balance of Competences review, the Crown Dependencies highlighted the importance of an EU Third Country policy that is aligned with international standards, is evidence-based, maintains investor confidence and is both transparent and consistent. Their specific recommendations included that:

⁷ The Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism - MONEYVAL

- impact assessments should more systematically expose any inconsistency between EU and international standards;
- the EU should use existing assessments by international institutions of Third Countries' compliance with international standards, and where assessments by international bodies are not available, should refer to existing peer review processes; where EU assessments of equivalence are still deemed necessary, the UK should have responsibility for determining equivalence in its dependent territories as the 'Member State of Reference';
- and in the event of delays in EU equivalence decisions, the UK should be able to establish or extend transitional measures for access to its own market.

The issues highlighted above would not alter for the Isle of Man in the event of a Brexit, as it is currently considered a third country for the purposes of financial services, and would continue to be so. However, were the UK to become a third country, then this may have an impact on (and potentially improve) the Island's ability to gain access to the UK market – or to put it another way, it may reduce the possibility that EU rules could limit access for third countries, such as the Isle of Man, to the UK.

Conclusion

The financial services industry is an important element of the Isle of Man economy, and it is therefore important that it continues to be supported and protected from external shocks. As with many external influences, however, the decision as to whether the UK chooses to remain in, or leave the EU, does not rest with the Isle of Man. The Isle of Man Government, and industry, can only react to the outcome of the referendum.

The Island's financial services industry has grown up effectively outside the EU, with access to EU markets historically restrictive. If the UK leaves the EU, then this may lead to increasing protection of the EU's single market – not only because of the loss of the UK as an advocate of free/liberal trade but perhaps to protect the EU's other financial centres from the City of London. Conversely, access to the UK could be potentially enhanced by the UK's enhanced freedom to negotiate terms with other third countries – including the Isle of Man – and its need to attract inward investment/funds from sources other than the EU.

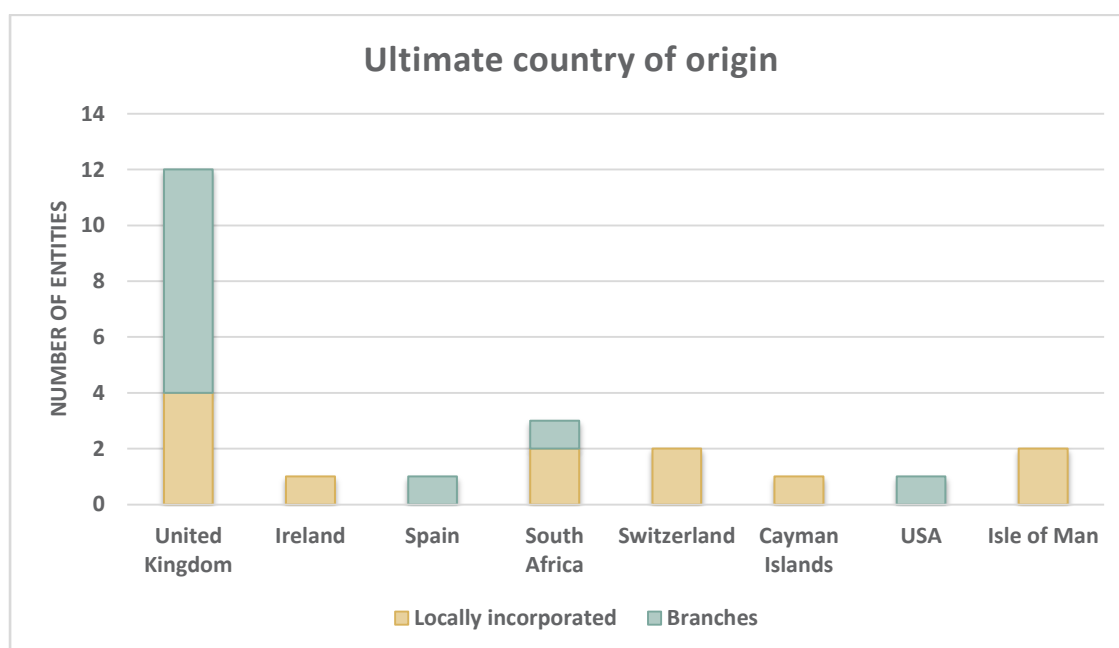
Appendix 1 – Assets and Liabilities of banks in the Isle of Man

£'000	Assets	Percentage of total	Of which, banks	Of which, non-banks	Percentage of non-banks	Liabilities	Percentage of total	Of which, banks	Of which, non-banks	Percentage of non-banks
All countries	45,053,990		37,841,267	7,212,723		45,053,986		12,384,103	32,669,883	
Unallocated	23,967	0	8,049	15,918	0	142,760	0	72	142,688	0
Isle of Man Residents	6,701,581	15	3,259,943	3,441,638	48	15,068,277	33	3,073,555	11,994,722	37
Non EU (includes Guernsey, and Jersey)	9,289,148	21	7,478,038	1,811,110	25	16,100,795	36	6,216,978	9,883,817	30
EU members excluding UK	1,340,573	3	1,135,589	204,984	3	2,214,435	5	105,684	2,108,751	6
United Kingdom (excludes Guernsey, Isle of Man and Jersey)	27,698,723	61	25,959,648	1,739,075	24	11,527,718	26	2,987,814	8,539,904	26

Data as at 30 Sep 2015, taken from returns made to BIS. Excludes one bank in the IOM.

Appendix 2 – extracts from the IOMFSA's quarterly statistical bulletin (banks) (30 Sep 2015)

Ultimate country of origin of banking groups operating in the Isle of Man



Geographical source of non-bank customer deposits

All currencies / entities:

		% of total
Isle of Man (a) Individuals	2,966,665	9
Isle of Man (b) Other	8,445,488	26
United Kingdom	9,295,161	29
Republic of Ireland	645,277	2
Other EU countries	1,429,085	4
European non EU countries	1,504,713	5
Middle East	1,211,782	4
Far East (including Japan)	1,019,432	3
North America (including Canada)	1,439,423	4
Other	4,263,809	13

7.b – Manufacturing

The manufacturing sector employs approximately 2,500 people primarily in three areas; precision manufacturing, food and drink, and general manufacturing. The sector accounted for 3.4% of the Island's National Income in 2013/14, and is an important element of the diversified economy the Isle of Man Government is seeking to nurture.

Precision Manufacturing

The Isle of Man Aerospace Cluster consists of 23 companies involved with aerospace design, manufacture or service provision and is a joint initiative between the Department of Economic Development and the Isle of Man Chamber of Commerce. Between them, these companies employ around 1000 highly skilled staff. This number has grown significantly in recent years and the Isle of Man Government is also continuing to invest heavily in supporting the development of locally trained engineers to help the sector achieve its anticipated growth projections.

Many of the companies based in the Isle of Man are subsidiaries or sister companies of larger UK or international concerns, and they manufacture components which feed in to the larger supply chain of what is a complex global industry.

The success of the Isle of Man Aerospace Cluster, combined with its status as a sister cluster to the North West Aerospace Alliance, means that it is now an integral part of the UK's aerospace sector supply chain. Cluster firms are directly involved in every major civil and defence aerospace project.

Food and drink

Taking the produce supplied by the agriculture and fisheries sector (see 7.c and 7.d below), the Isle of Man food and drink sector contributes around £75m⁸ to the local economy as well as providing jobs in catering, processing/manufacturing and merchants (600 jobs directly with another 1,000 in the supply chain (fishing boats, ingredients, logistics, marketing).

While much of the Island's produce is destined for the domestic market, high quality food and drink including cheeses, meat, seafood, ice cream and beer is also exported to the UK and further afield.

General manufacturing

The sub-sector is very diverse, producing a range of goods from shaving brushes to anchors. It represents 900 jobs and serves most global sectors, exporting to a blue chip company base.

Isle of Man manufacturing exports

The Customs and Excise Agreement, VAT sharing arrangements, and Protocol 3 (see sections 3 & 4 above) have supported the development of a significant high tech manufacturing sector on the Island. Whilst the sector may be relatively small in terms of its contribution to the Island's national income, its contribution to the local economy and the community is significant, providing a broader variety of employment and training

⁸ Source DEFA Food Matters Strategy

opportunities, and also, providing for greater economic resilience for the Island economy as a whole.

Aerospace products are exclusively destined for export, as are the majority of those in the general manufacturing sector. Protocol 3 and the Customs and Excise agreement allow manufacturers of goods produced in the Isle of Man to access the EU's single market, as well as exporting to the rest of the world on the same basis as those manufacturers producing within the EU. For example, goods manufactured in the Isle of Man attract no tariffs when exported to the EU (including the UK), and similarly, enjoy the same preferential treatment when exported to say, Korea, with which the EU has a Free Trade Agreement. (In addition, further EU trade deals with Canada, the US, and Japan, which are currently in the pipeline, will increase the scope for trade even further).

What would be the impact on the Isle of Man of a UK vote to withdraw from the EU?

As is noted in the introduction to this report, there is no clear consensus as to whether the UK leaving the EU would be beneficial or harmful for the UK economy, and there are many studies, reports, polls and surveys which support the arguments to 'remain' or to 'leave'.

In terms of the manufacturing sector, there is a little more clarity than there is in other areas. It is argued by some that approximately three million (UK) manufacturing jobs are reliant on access to the EU Single Market. Others state that it is not the case that if the UK withdrew from the UK those jobs would simply be lost and that it is possible that companies which currently export their goods to the EU may well be able to do so in the future.

Two issues, however, are relatively certain –

- Firstly, goods sold in (to) the EU Single Market would continue to be required to meet the relevant EU standards in terms of the labelling, quality, product safety, etc. which are determined by the EU and also may be subject to tariffs/quotas etc; and
- Secondly, export of goods to countries with which the EU has a trade agreement might, should the UK be outside the EU, attract tariffs which are not currently levied on products emanating from within the EU (albeit that World Trade Organisation rules must be adhered to).

Most UK manufacturers have asserted that whilst the EU is far from perfect, to leave would render British exports to Europe more costly, and also potentially introduce additional restrictions for British exporters, which their European competitors may not have to contend with.

The UK Aerospace, Defence and Space Industry representative body ADS (of which the Isle of Man Aerospace Cluster/DED is a Member) released the results of a poll in the summer of 2015 which showed that only 2% of their 900 membership (which includes BAE systems and Rolls Royce) recommended the UK should leave the EU. Similarly, the CBI has stated that it is the view of the majority of its members that the UK should remain in a reformed EU, as British industry depends on free and open trade. The British Chambers of Commerce EU Business Barometer showed (for Q1 2015) that 63% of firms (out of 3,800) surveyed believed that "*withdrawal from the EU will have a negative impact on Britain's business and economic impact*". BCC Members did agree, in the same way as CBI Members, that the EU required reform, and they supported the UK Government's policy of renegotiation and referendum.

There are, however, some prominent voices within UK industry who believe that the interests of the UK would be better served by leaving the EU. The groups 'Business for Britain' and 'Leave.EU' (along with others) have been lobbying business leaders, as well as the CBI, to adopt a more critical or Eurosceptic position.

Those who advocate that the UK should leave the EU suggest that EU rules ('red tape') are restrictive and mean that UK businesses incur additional costs as a result of EU membership. They also feel that EU employment rules make it more difficult for companies to keep employment costs low, with the Working Time Directive often cited.

These issues do not apply to the manufacturing industry alone.

In terms of the Isle of Man's manufacturing industry specifically, and without indulging in speculation, four key observations can be made;

- Firstly, the majority of Isle of Man goods are produced for export. Although they are predominantly exported to the UK, many of those goods may then be sold onwards to the rest of the EU – for example the components supplied to the aerospace industry will ultimately be fed in to the global supply chain, and certain food products (especially fisheries products) sold to merchants/suppliers in the UK are destined ultimately for the European market. Isle of Man manufacturing businesses would be affected by any arrangement that leads to additional checks or paperwork. They also could no longer be seen to be on the same playing field as other producers across the EU.
- Secondly, the future success of the Isle of Man manufacturing industry will, in large part, depend on the future viability of partners in the UK. In respect of the aerospace sector in particular, the Isle of Man Aerospace Cluster is a sister cluster of the Northwest Aerospace Alliance and many companies are closely aligned with their partners and/or parent/sister companies in the UK.
- Thirdly, the UK's future relationship with the EU (and the subsequent character of the Isle of Man's relationship) will determine the impact on the Island's manufacturing sector. Although outside of the EU, the manufacturing industry is – by virtue of the Customs and Excise Agreement, and Protocol 3 – able to operate as if the Isle of Man were part of the EU. It is in this sector (and agriculture & fisheries) therefore, that the effects of a UK exit from the EU may be most profound. If the UK leaves the EU, but is successful in negotiating access to the Single Market, then it may well be that there will be less significant change, but the UK may still need to secure trade deals with many other international partners. What is crucial for the Isle of Man is that it makes it clear to the UK what it would wish to retain/gain in the future.
- Fourthly, uncertainty about the future may have a significant impact on the UK and Isle of Man economies, and may affect investment decisions. This is doubly important for the Isle of Man, as not only will there potentially be uncertainty about the UK's future relationship with the EU, but in addition to that, how the Isle of Man may seek to be a part (or not) of that future relationship.

Conclusion

The manufacturing sector relies more than most others on the Island's existing relationship with the UK and the EU. Clearly, therefore, it is this sector where there is more risk to the Island economy, should those relationships be altered. Should the UK determine to leave the EU, then the Isle of Man Government will need to ensure that the UK Government is aware of the importance of the Isle of Man manufacturing industry, and also, to continued access to the UK and EU markets.

7.c – Agriculture

The agricultural sector employs 754 (in 2011) people across the meat, dairy and arable sectors.

Meat

Data from the 2015 census gives, figures for breeding females (calved cows and in calf heifers) to be 12,388 cattle (43% of which were dairy breeds), 51,000 sheep that had lambed, and 271 female breeding pigs. The red meat sector accounts for 85% of active farmers (those claiming ADS payments) with 341 individual holdings carrying livestock which could be used for human consumption on the Isle of Man in 2015

The proportion of animals which are processed on the island is largely governed by price paid by Isle of Man Meats (IoMMs) for the livestock. In 2014 62% of cattle (5.9k), 88% of sheep (41k) and all the pigs (3k) were slaughtered locally: IoMMs is the only processing facility for the slaughter of Manx-produced meat.

In 2014 IoMMs processed and sold £9.5m of locally produced meat (£9.9m including the value of hides etc). As a percentage of meat sales value, 42% was sold locally, and 58% exported. Beef accounted for 64% by of total production by value (with 41% by value consumed locally, and 59% exported), sheep for 30% (25% local consumption and 75% export) and pigs 5% (98% for local consumption).

Clearly, although much of the meat produced on the Island goes to local consumption, the industry relies on exports sales for the majority of its income for the beef and sheep industries. The majority of these sales are to the UK, with sales of meat to rest of the EU, including Ireland, channelled predominantly through the UK.

Dairy

The dairy sector accounts for 32 of active farmers in the Isle of Man. In 2015 there were some 3,796 dairy cows on 32 dairy farms producing a predicted 20 million litres of raw milk. All milk is processed by Isle of Man Creameries which operates as a farmers' co-operative.

Local liquid milk sales accounted for one third of milk produced, with cheese and butter accounting for the rest. The dairy processing sector accounted for £13.6M of sales in 2012, with the domestic market accounting for around 61% and exports, the remaining 39%.

Whilst the sale of local milk remains the most profitable element of the industry, this has seen a decline due to competition from imported milk through local supermarkets.

In terms of destination of exports, commodity milk is sold to the UK, and there is some branded cheese being sold directly to the US and Canada.

The key issue for the industry is to maintain a critical mass of at least 15 to 20 million litres of milk, and this is dependent upon the ability to retain and grow the share of local liquid milk sales, as well as increase the volume and value of branded and artisanal cheeses.

Cereals

The cereals are grown by 24% of active farmers although those growing Milling wheat (12) account for less than 3% of farmers in the Isle of Man. In addition, Laxey Glen Mills employs 8 staff and Ramsey Bakery 80 staff. Latterly, Noa Bakehouse has also come to be viewed as a small but important part of the local supply chain; both Ramsey Bakery and Noa place high value on the local provenance of their product.

Locally grown milling wheat is sold exclusively to Laxey Mills and the flour produced is all sold locally. Some milling oats are produced (1500 tonnes in 2015) which are exported under a contract negotiated with Isle of Man Farmers to the UK.

Eggs & poultry

There is only one free-range chicken producer operating on a small scale. Some 82 claimants declared that they had hens on their holdings although of these only 14 had a hundred birds or more and one flock contained more than half of the nations declared stock of 13,000 birds. This produce is largely sold on-Island.

Potatoes

Potatoes were grown on 268 acres by 20 growers, but this produce is destined largely for local consumption as their export is uneconomical.

Vegetable & horticulture

The vegetable sector operates on a smaller scale and production is confined predominantly to 2 growers one who grows 45 acres of mixed veg the other approximately 9 acres. Horticulture (plants and herbs) now take up an extremely small area and none of this produce is likely to be exported.

Regulation EC/706/73, animal health & support measures

In addition to Protocol 3, Regulation EC/706/73 introduced further specific measures to ensure that agricultural products could continue to be traded freely between the Isle of Man and the UK, and from that point, throughout the EU.

The Regulation states that –

- the rules applicable to the UK for trade in agricultural products covered by Annex II of the Treaty (and goods covered by Regulations 170/67 and 1059/69 – certain products processed /made from agricultural products) also applied to the Islands with the exception of rules on refunds and compensatory amounts granted on exports by the UK
- For the purposes of these rules, the UK and the islands were deemed to “be treated as a single Member State”

- No refunds or compensatory amounts was to be granted in respect of the products referred to above originating or coming from the Islands in respect of which customs formalities are completed in a Member State
- Where these products are exported to EU Member States or to third countries, the Islands could not grant aid in excess of that granted in the UK
- Rules on State Aids shall apply in relation to these products
- Community rules in respect of the following shall also apply in relation to imports/exports to/from the Islands, as they would in the UK
 - Veterinary health
 - Animal health
 - Plant health
 - Marketing of seeds and seedlings
 - Food legislation
 - Feeding stuffs legislation
 - Quality and marketing standards

To a large extent, therefore, in relation to agricultural produce and products derived from them, the Isle of Man is treated as if it is part of the EU (the UK). Whilst this could be deemed to introduce the need to comply with excessive administrative or other burdens, in strict terms this only applies to products which are exported to the UK and the rest of the EU. In addition, even if the Isle of Man were outside the EU, these requirements would need to be met in order to continue to export to EU Member States.

There is also an added advantage in that the Isle of Man can benefit from free access to markets beyond the EU on the same terms as EU Member States, as its products are recognised as meeting EU standards. In addition, trade deals negotiated by the EU on behalf of its Member States extend to cover the Islands to the same extent as Protocol 3.

Food security & countryside management

Whilst in economic & employment terms it could be argued that the agricultural sector is less important than other sectors, there is a strong rationale for protecting and supporting the industry, in that food security is important for the future sustainability of the Island, as well as the value of the industry to the visitor economy (the landscape, and local produce) and the desire of the Isle of Man Government to maintain a diverse and broad base to the local economy.

Labour

The agriculture industry has, traditionally, utilised a high proportion of seasonal and/or casual labour, and in the UK, much of this labour is sourced from central and eastern Europe.

The (UK) National Farmers' Union publication "EU Referendum – UK Farming's Relationship with the EU" states that whilst access to the single market is important, "it's an absolute priority that British farmers and growers have access to non-UK born labour to carry out all their operations". Whilst the NFU does not come down either in favour or against the UK remaining the EU, it is clear that they believe that the ability to source casual and seasonal labour is vital to the industry.

Conclusion

As outlined above, the agricultural industry in the Isle of Man benefits from a deep integration into the EU Single Market, and also benefits from being treated as if it were part of the UK in relation to exports into the EU and beyond.

Some may argue that the additional requirements in relation to the limits placed on aid which can be provided for farmers/state aid, application of rules on animal health etc. and an inability to access EU support measures means that the disadvantages may outweigh the advantages.

However, the evidence suggests that whilst much of the agricultural produce is consumed on Island, the ability to export to the UK and further afield is important to the beef, sheep/lamb and dairy industries on the Island, and that a significant proportion of farmers' income derives from exports.

If the UK were to leave the EU and Protocol 3 were to cease to have effect, it would therefore be necessary to negotiate access to the UK market, at the very least, in order to ensure the viability of the Island's agricultural industry.

7.d – Fisheries –

Overview

The Manx Territorial Sea extends to 12 nautical miles (or the median line between the Island and the UK/Ireland) and covers a total area of 4,000km².

The Isle of Man is not part of the EU, and is not therefore directly subject to EU fisheries policy, including the Common Fisheries Policy. However, for historic and constitutional reasons, although Isle of Man territorial waters are governed by Manx legislation, this must be compliant with the Fisheries Management Agreement (FMA) between the Isle of Man and the United Kingdom – an agreement which allows for access to Manx waters for UK fishermen.

It states that fisheries matters in the extended territorial sea (3-12nm) must comply with the UK's obligations under the Common Fisheries Policy (CFP). The exact wording states that Manx rules and regulations must be consistent with the UK's under the CFP, and in addition, the Isle of Man can impose additional conservation measures either by legislation or licence condition. The FMA does not apply to inshore (0-3nm) waters, but within the extended territorial seas, it requires fair and non-discriminatory access for UK vessels and Manx vessels in turn have fair access to UK waters.

Protocol 3 (Article 4) stipulates that the Isle of Man must not discriminate between nationals of different EU Member States, and as a consequence, the Isle of Man rules must be concurrent with the Common Fisheries Policy, meaning that the catch in Isle of Man waters is set against EU quotas (where those rules apply), rules on fishing gear/methods must be applied, along with other rules governing fisheries conservation.

The London Convention 1964 stipulates the access agreements for non UK vessels fishing commercially in the Manx territorial sea – so Republic of Ireland, Belgian and French vessels have restricted access for fishing for certain species between 6-12nm of the territorial sea. Only certain EU flagged vessels can fish in some areas. At this point in time, it is assumed that as the London Convention was signed before UK became a full member of the EU, this arrangement would be likely to continue should the UK withdraw from the EU.

The Manx Fishing Fleet & Current Production

Sea Fisheries, which includes onshore processing, is currently worth an estimated £12m per annum to the Manx economy and provides around 400 jobs (IoM Government 'Food Matters', 2014). A significant proportion of the fisheries effort in Isle of Man waters is undertaken by vessels operating out of Scotland and Northern Ireland for scallops and some Northern Ireland vessels for pot fishing, although the Manx fleet itself consists of a total of 64 licensed vessels, of which 30 target either, or both scallop species, 33 pot for crab, lobster and whelk and 1 is exclusively fin fish.

Currently, the four main species of shellfish commercially exploited from the Manx territorial sea are queen scallop, king scallop, crab and lobster. There is increasing interest in a local whelk fishery and other species such as squid are landed in small quantities. Very few fin fish (such as cod, herring, mackerel etc.) are landed due to low market value, low demand or lack of quota for the species.

Local landings are dominated by queen scallop and king scallop, with crab, whelk and lobster making up the rest. Fin fish and langoustine (*Nephrops norvegicus*) make up a very small proportion of local fishery production.

Home & Export markets

The majority of King and Queen Scallops landed to Manx processors are exported to France and Spain; most of which are not currently differentiated as being Manx. With respect to crabs and lobsters, one company accounts for 80% of the catch and most is exported live to the UK, for onward transport to the Far East. The remainder is sold on Island via fishmongers or direct to caterers. Both whelks and langoustine are export products, with Asian and European markets being the main customers.

Fishery and landings data collected by DEFA suggests that around 90% of lobsters landed by Manx boats are exported live, whereas 75-80% of brown crab is exported, the remainder being processed and consumed locally.

UK exit from the EU – potential effects on the Isle of Man industry

On the face of it, the impact of the exit of the UK from the EU may be significant to the fisheries industry, as much of the catch is sold to the UK, Europe or Far East.

In particular, French, Spanish and Italian markets for queen and king scallops may be affected by the need to satisfy additional rules or external tariffs, as the Isle of Man would then require third country access to the EU Single Market. This could result in an increase in

the price of Manx produce. In the event that the UK does leave the EU, however, the possibility that it will not secure access to EU markets for trade in goods is considered unlikely by industry.

The direct sale of Manx produce is only one possible impact. There may also be an effect upon UK buyers (of Manx produce) who in turn see their costs/administrative burden increase. Additionally, access to overseas markets could be affected indirectly as Manx produce would no longer be viewed as originating from the EU, and could be subject to additional tariffs, administrative costs, or health/safety checks (e.g. heavy metals, organic chemicals (PAHs) and phycotoxins).

Fisheries product	Current market	Potential impact if UK withdraws from EU
Brown crab	Sold primarily to UK	Possible direct export to Asian markets in future, which could be affected.
Lobster	Sold primarily to UK (possibly then on to EU)	Secondary effect via the UK is possible.
Whelk	Exported to Europe and SE Asia	Unknown effect on exports to Asia (but if IOM seen to be outside EU compliance, then potentially additional testing required) (similar to live crab).
King scallops	70% to France, 10% to Spain, 10% to Italy & 10% to IoM	Potential disruption of sales to the EU
Queen scallops	40% to France, 30% to Spain, 20% to Italy and 10% to UK/IoM	Secondary effect via UK buying practices and if Protocol 3 rescinded, then potentially additional testing to sell to EU markets.

The Isle of Man has developed a good working relationship with the UK Fisheries Administrations which has been built up over a few years. However, should the UK withdraw, a re-negotiation of the Fisheries Management Agreement would be essential, and more flexibility and freedom to manage our own waters would be welcomed by the Isle of Man.

7.e – e-Gaming

The e-Gaming sector in the Isle of Man has grown in size and significance to a point where it contributed 16.7 % of the Island's National Income in 2013/14, and provided employment for 900 people.

In addition, other professional and technical services, including lawyers, accountants and corporate service providers, and software providers/developers and disaster recovery services and IT/telecoms rely to a lesser or greater degree on the sector. Salaries in the e-Gaming industry are generally high, and the sector has provided much needed growth during a period when other sectors of the economy have performed less well.

Whilst there is no data collated which can pinpoint where customers of Isle of Man based e-Gaming companies are situated, it is predominantly international (non-European) markets to which Isle of Man companies' products are targeted/marketed.

The EU does not regulate the e-Gaming sector, and competence in this area is retained by individual Member States. Consequently, the actions of individual Member States are what will determine access for Isle of Man companies to markets/customers in each of the EU Member States, with some imposing more restrictions than others. In 2014 the Isle of Man introduced a Double Duty relief facility for Isle of Man based operators who found themselves liable for duty in (primarily) the UK, and other EU Member States.

If the UK were to vote to leave the EU, it is likely that there would be a minimal impact on the Isle of Man providers of e-Gaming services, and as with other sectors, it is the future relationship with the UK (arrangements in relation to VAT) which will be of greater significance. Similarly, the ability to attract skilled workers may well be a factor for future growth in this sector.

7.f – Maritime sector

Overview

Although a traditional register of ships has existed since 1786, the Island's modern shipping sector was established in 1984 when Isle of Man government created an International Register. This coincided with extension of the relevant International conventions to the Island by the UK, and Isle of Man Government employed the services of a Chief Marine surveyor to set up a Maritime Administration (now the Isle of Man Ship Registry). This was at a time when UK-based companies were "Flagging Out" their ships and leaving the UK for places such as Hong Kong, Bermuda and Cyprus. The Isle of Man sought to take advantage of this situation offering a register closer to home and located in a European time zone to set up and operate from. It attracted companies like Shell, Anglo Eastern, Canadian Pacific, Denholms, from the UK, and also companies such as Doehle (as Midocean) and Bernard Schulte (as Dorchester Maritime) from Germany.

Yacht management grew from the mid-90s onward in the private sector and was introduced as an option for registration of super-yachts in the Ship Registry from 2003 onwards. This is now a distinct subsector of the maritime industry on the Isle of Man.

The sector today is quite diverse and employs some 580 FTE with almost 100 of this headcount in the commercial yacht sector. According to the 2013/14 National Income Accounts, the Shipping Sector contributed £105,494,763 to GDP, which is around 2.4%.

International relations/relationships

With regard to the operation of an international register, the UK is the 'Flag State' at IMO (International Maritime Organization) and represents the Isle of Man internationally. The delegation which enables the Island to operate an international register is derived from the UK's 1995 Merchant Shipping Act which provides for the central register of British ships on the UK Ships Register. Section 18 of Part II of the Act, allows by Order in Council, British possessions (both CDs and OTs) to establish different categories of register with restrictions on vessels according to the tonnage, size and type. The Isle of Man is a Category 1 register which has no limits.

If the UK were to leave the EU (Brexit,) it is not envisaged the position of the Island in relation to the IMO would change. The UK's relationship with the EU has no bearing on its member status at IMO or ILO. In fact the UK could assume a much more independent role at IMO, without concern for EU sensibilities, competence, and direction. The UK

representative may be able to better represent the Isle of Man (as a non-EU British Flag Administration) at IMO which could also be to the Island's advantage.

Implications UK withdrawal from the EU

It is unlikely that there would be any problem for Isle of Man registered vessels trading into/out of EU ports. Shipping is an international business with over 130 Flag States, of which only 27 are EU member states. Europe needs international trade and has to tread a careful path with unilateral requirements which could inhibit trade. If the UK did withdraw from the EU, the Isle of Man's position as a non-EU Flag would remain unchanged and the UK would also become a non-EU Flag.

For commercial yacht business on the Isle of Man the effects would be markedly different. UK withdrawal from the EU could mean the loss of favourable UK/EU VAT arrangements and access for commercial yachts with the potential loss of this business from the Isle of Man to places such as Malta as a favourable EU yacht jurisdiction. This would almost certainly see the loss of the majority of yacht business, which is the core function of many CSPs, in a sector currently employing about 100 people.

The withdrawal of the UK from the EU would mean that in the merchant shipping sector with regard to vessel registration and supporting professional services, the UK could lose many of the advantages of being a EU Flag in terms of tonnage tax incentives and access to cabotage trade in Europe. Hence there would be no advantages of registering in UK over the Isle of Man. This could be very positive for business and registration in the Isle of Man as it provides a more client-focused and pragmatic alternative to UK registration.

7.g – Aircraft

The Isle of Man Aircraft Registry was established to provide for the registration of high quality private and corporate jets and high quality twin turbine-engine helicopters. Isle of Man registered aircraft cannot be used for Commercial Air Transport. Supported by a contract with a UK based aviation safety consultancy, the register engages twenty Surveyors resident in Central Europe, USA, UK and the Isle of Man, which enables it to provide an efficient and cost-effective service.

At the start of July 2015, only 8 years since the register was established, the register welcomed its 800th aircraft with 460 aircraft currently active on the Register.

As with the yacht register above, and flowing from the creation of the aircraft register, the Corporate Service Provider sector provides professional services for the ownership and management of aircraft. It is because the Island is treated as part of the European Union for VAT and customs duty purposes that Isle of Man companies can be part of United Kingdom VAT groups and aircraft can be imported – into the EU – via the Isle of Man, making use of the VAT regime and aircraft owning structures. The ability of the Isle of Man to provide for companies which can own and control valuable assets, such as aircraft, and allow for VAT registration is a strong selling point for the sector.

In addition, aircraft held in Manx companies which are VAT registered are often flown to Ronaldsway. A loss of the favourable regime which supports this sector would mean that air traffic could be reduced resulting in loss of revenue to the airport and local businesses.

Some Isle of Man based operators also have sister offices in the UK and the rest of Europe, and there is concern that UK based operations could also be adversely affected by UK withdrawal from the EU, with consequent knock on effects for the Island.

7.h – Tourism & the Visitor Economy

Tourism and the broader Visitor Economy provide a valuable contribution to the Isle of Man's economy and quality of life and is a significant source of local jobs.

Total visitor spend amounted to £108 million in 2015 providing income to and generating employment for carriers, accommodation providers, attractions, eateries, and retailers.

The visitor economy helps to support local businesses in providing a broad range of services (restaurants, bars and cafes) as well sports and leisure activities (sports facilities, special events) including the world renowned TT races.

Transport links are primarily with the UK (some with Ireland) and there are no direct services to continental Europe (with the exception of some chartered services during the Summer, provided primarily for the local market)

EU competence in the field of tourism is very limited, and although some EU funds do go to support cultural or educational events, the improvement of transport links, ports/airports, roads and other infrastructure which improve connectivity and support visitor travel, none of these funds is currently available to the Isle of Man.

While journeys to and from the Island are made easier by the fact that the Island shares a common currency with the UK, is part of the EU customs union, and also a part of the Common Travel Area with the UK, Ireland and the Channel Islands, it is difficult to envisage there being any significant impact upon the number of people visiting the Island if the UK left the EU.

Free movement of people, the future of the Common Travel Area and the Customs Union are all discussed elsewhere in this report, and so it is perhaps sufficient to say that if the UK were no longer a Member State of the EU, then it may be the case that travel to and from continental Europe might become more difficult, and therefore result in an increased in tourism business within the British Isles.

7.i – Energy

Oil & Gas

The Isle of Man currently imports all gas and petroleum products direct from the UK. In turn the UK imports around 50% of its fossil fuel energy requirements from global markets, with a sizeable contribution from Europe especially Norway. The UK has recently invested and is expected to continue to invest in new liquid natural gas (LNG) terminal facilities to enable access to global gas markets. The Isle of Man has a connection to the Scotland/Ireland interconnector gas pipeline which supplies natural gas to the Island.

The EU Directives allow non-member states, such as the Isle of Man, access to gas network standards and connections. Should the UK decide to leave the EU, there is uncertainty as to how the UK would facilitate connections and trade with neighbouring European countries. Presumably a negotiated agreement between the UK and the EU would allow continued connections and trading arrangements and it is therefore unlikely that it would have a significant impact on gas and petroleum imports to the Isle of Man.

Electricity

The UK currently has electricity connections to neighbouring EU grids in France, Holland and Ireland. Further interconnectors are planned to Norway, Denmark, France and Ireland in the next 5 years which will further strengthen the grid resilience of the UK. The Isle of Man has a subsea cable connection to the UK which allows the Island to trade electricity with the UK. As noted above, in relation to gas infrastructure, there is uncertainty regarding the impact on the Isle of Man. However, a negotiated agreement between UK and EU would allow continued connections and trading arrangements and it is therefore unlikely that it would have a significant impact on the Isle of Man.

The EU Renewable Energy Directive sets targets for all member states, including a target for the UK to produce 15% total energy from renewable sources by 2020 and a commitment to increase share from renewable sources post 2020. This created an opportunity for the Isle of Man to develop offshore projects to potentially export renewable energy to the UK to assist with meeting the target. There is uncertainty on the potential impact for the Isle of Man should the UK no longer be an EU member and therefore no longer have the EU renewable energy target. The UK would still have the legal requirements in the Climate Change Act and an obligation from the recent United Nations COP21 agreement to deliver clean renewable energy. Therefore, it is likely that the UK would still require cost effective renewable energy generated from the Isle of Man.

Conclusion

It is uncertain what the full impact for the Isle of Man energy sector would be should the UK referendum result in the UK deciding to leave the EU. It is unlikely that energy supplies would be impacted however, the Isle of Man Government would need to further discuss possible implications with the UK Government.

8. Provision of Government Services – Departments

8.a – Department of Education & Children

The Department of Education and Children operates the Island's 37 schools – 32 primary and 5 secondary – and the Isle of Man College of Further and Higher Education⁹, which offers professional, exam/degree and recreational courses for adults. It works with other Government Departments and agencies to deliver services for children, including safeguarding and needs-based assistance and the Department also runs the Youth Service.

The Department does not envisage that there would be a significant impact upon its ability to provide these services, if the UK voted to leave the EU.

In terms of the operation of the Island's schools, there would be no change in the Department's ability to access the services of external examination boards (curriculum, exams, etc.) which is currently undertaken on a commercial basis. The current system of peer-review based assessment of schools/teaching standards is similarly undertaken on a commercial basis with a UK company. The Department accepts teachers who are qualified in the UK under UK rules, as being qualified to teach in the Isle of Man. The only difficulty which may arise is the possibility that changes to rules governing free movement of people may restrict the ability to employ teachers who are EU (non-UK) nationals, including from

⁹ University College Isle of Man (UCM), from 1 April 2016

Ireland, which may well cause problems with recruitment. This may be especially relevant in recruiting teachers of modern languages.

The DEC maintains a 'Bilingual Service' with a budget of £184k, to support children to learn English, where English is an Additional Language. The Service is headed by an Advisory Teacher who co-ordinates the work of a small team of bilingual Education Support Officers. These Officers are deployed across primary and secondary schools on the basis of levels of need - with priority given to those children who are completely new to English.

For students educated in the Isle of Man, access to universities in the UK would be unlikely to alter, and although few attend EU universities, these students would not see a change in their status, as they are already classed as 'third country' applicants. However, it should be noted that potential changes to rules allowing for free movement of British citizens, should the UK leave the EU, may well have an impact on Manx students wishing to live and study in the EU.

8.b – Department of Home Affairs

The purpose of the Department of Home Affairs (DHA) is to ensure community safety in the Isle of Man. The operational services of the Department are:

- Isle of Man Constabulary (including Emergency Planning and Civil Defence)
Isle of Man Fire and Rescue Service
- Isle of Man Prison and Probation Service and
- Communications Division

Whilst each of these services maintains close links with its UK counterparts, the connection to EU rules and/or institutions is less close.

The links between the Isle of Man and UK police forces are complex, and largely informal. There is reciprocity on pay and conditions, and training is either carried out in the UK, or is undertaken on-Island to UK standards or accredited through UK bodies, such as the College of Policing. The Isle of Man Constabulary is not compelled to take this stance, but does so in order to allow for the Island's and UK's police forces to be able to work together whenever necessary. Having similar standards, practices and protocols allows for more effective co-operation. The UK's National Crime Agency (NCA) is obliged (under UK law) to assist the Isle of Man if requested to do so. The Island's Chief Constable attends meetings and participates in the work of the National Police Chiefs' Council, again, allowing for greater co-operation and mutual assistance. In addition, specialist equipment is usually purchased to meet Home Office standards.

The Europol convention does not cover the Isle of Man and European arrest warrants do not apply on the Island. Any legal assistance provided to European jurisdictions is given under the terms of the various mutual legal assistance treaties in place. Arrests carried out in the Isle of Man for offences which may have taken place elsewhere can only be undertaken by way of formal extradition, and this process is carried out by the Metropolitan Police Service. In practical terms, this means that when a formal request is made for the arrest and extradition of an individual, Isle of Man Constabulary would execute the arrest warrant and the Metropolitan Police Service would send officers to the Island who would then escort the offender to the Central Criminal Court for extradition proceedings.

The Island's Financial Intelligence Unit (FIU – which reports to Her Majesty's Attorney General's Chambers) is a member of the Egmont Group worldwide group of financial

intelligence agencies which helps to develop co-operation and the establishment of common standards in terms of mutual assistance in the sharing and development of intelligence in connection with financial crime, money laundering, corruption and the financing of terrorism. In relation to non-financial crime, the Isle of Man will share intelligence with law enforcement bodies across the world, either through Interpol (to which the Island has links through the NCA) or via direct contact with sovereign states. In relation to European countries, this includes – but is not confined to – contacts via the police liaison officers in the various Embassies and similar arrangements apply with other countries, including the US and Canada. One area where the Isle of Man is working with European Partners is in relation to cyber-crime, where Isle of Man officials are participating in an EU project. As a ‘third country’ for these purposes, this co-operation may be able to continue, even if the UK did leave the EU.

The Isle of Man Fire and Rescue Service (FRS) bases certain criteria for staff entry qualification and promotion upon UK standards (Behaviourally Anchored Rates Scales – BARS – and Personal Quality Attributes – PQAs). Off Island training is generally provided at the UK Fire Service College which is both a European and worldwide facility. External inspections of FRS can be undertaken by the Scottish Fire and Rescue Service, and additional Health and Safety peer reviews do also occur, following the RoSPA model. Fire appliances, uniform and equipment conforms with EU standards where applicable.

The Isle of Man prison and probation services do not anticipate any obvious impact should the UK vote to leave the EU.

The services provided by the Department of Home Affairs are internal to the Island, although there is a degree of co-operation with counterparts in the UK, there is little or no direct relationship with the EU. In addition, the UK itself maintains a number of ‘opt outs’ in the area of justice and home affairs, and consequently, the effects of a potential UK withdrawal from the EU would not be as significant as they might be in other areas.

8.c – Department of Infrastructure

The Department of Infrastructure provides a diverse range of services for the Manx community including highways maintenance and improvement works, planning policy, mapping, waste management, air and sea port facilities, properties and asset management, public transport, coastguard search and rescue, the provision of quarries and raw materials to support infrastructure development and the construction industry.

The Department also has responsibility for engagement with local authorities.

The majority of these services are internal to the Island, and are not impacted by the UK or Isle of Man’s formal relationship with the EU. One area, where there may be a considerable indirect impact is in relation to the provision of air services.

Air and Sea links

The EU has wide competence in matters relating to aviation as part of a wider transport policy. From 1987, in order to create a single market for air transport, the EU started a three stage process of liberalisation in the air transport sector, with completion of the single aviation market effectively completed in 1992. During this period, the UK played a leading

role in driving forward the development of the Single Market in an effort to open markets, foster greater competition, and deliver benefits to UK businesses and consumers.

Air transport is an area of policy which, according to the CAA^[1], the UK has usually found itself aligned with the Commission in promoting a liberal market-based aviation sector with high technical standards, making efficient use of available capacity.

In parallel with the setting-up of the Single Aviation Market, 'Common Rules' have been adopted to ensure its proper functioning, which requires, notably, a level playing field and a uniform level of protection for passengers. These are international standards, with rules applying to countries within the Single Aviation Market and providing basic international standards.

Although the Isle of Man is not included within the scope of such measures, all journeys to and from the Island will begin or end in EU (with rare exceptions, such as direct flights to Channel Islands, or Geneva). It is, therefore, the case that airlines will be subject to their requirements.

Major airlines operating between the Isle of Man and the UK, including EasyJet and British Airways, have stated that they would wish to see the UK remain in the EU, and envisage that it may be more difficult for airline operators if the UK were to leave. Some airports, including Heathrow and Gatwick, are also of the same opinion.

EU rules relating to operational and safety standards do not automatically apply to the Island, but are adopted as good practice or as a consequence of the Isle of Man's close working relationship. With regards to Aviation Security, the Isle of Man has already adopted EU rules and has third party status. In addition, the Isle of Man must be mindful that measures taken on Island cannot be deemed to be considered illegal state aid.

If the UK were to leave the EU, then there would be a need for the UK to reach agreement with the EU as to the operation of air services to and from the EU, as a third country, and the Isle of Man would need to ensure that it was included within these negotiations.

8.d – Department of Health & Social Care

Health care is an area in which the EU is generally limited to a supporting role and it is recognised in the EU Treaties that Member States are responsible for their own health policy, for the management and delivery of health services and medical care, and the allocation of the resources assigned to them. The EU's role in respect of social care is extremely limited.

In the Isle of Man it is the Department of Health and Social Care which is responsible for providing the resident population of the Isle of Man with –

- Acute care (secondary health care at Noble's Hospital & referrals to tertiary centres in the UK)
- Community care (primary health care through clinics, community health workers, mental health care, adult social health care and children and families social care: and a network

^[1] CAA submission of evidence to Balance of Competence review – see https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/278966/boc-transport.pdf, p.13

- of commissioned services including general medical practitioners, dentists, optometrists and pharmacists)
- Public health services

Health care is provided only to those who are 'ordinarily resident' in the Isle of Man. However, there are a number of exceptions in respect of the types of treatment covered by this provision (including emergency treatment) and of those persons who are covered (including those working for an Isle of Man employer).

In addition, this area is bound by a number of International Conventions, and there are also some (bilateral) reciprocal health agreements in place. Those people who are 'ordinarily resident' in the Isle of Man do not benefit from the EU's EHIC (European Health Insurance Card) provisions and must therefore take out travel/health insurance when travelling in the EU.

The EU also has a limited role in relation to public health, and other health related areas linked to the single market. These other areas/measures include –

- Medicines
- Medical devices
- Organs, blood, tissue and cells
- Nutrition and labelling
- Tobacco
- Alcohol
- Health security
- Radiation
- Public health programmes
- Rare diseases
- Implications of employment policy (specifically the Working Time Directive)
- Free movement of persons (health care professionals and recognition of their qualifications, coordination of healthcare and particularly the benefits which support access to healthcare, and the cross-border provision of healthcare services)

Under the very limited scope of Protocol 3, the majority of the measures adopted by the EU in the field of health care are not applicable in the Isle of Man, but many will be relevant due to the Island's close links with the UK national health service, participation in the single market, and indeed some measures which are adopted as good practice. If, for example, an Isle of Man based manufacturer wished to produce and sell medicines, medical devices or health foods, then it must comply with EU rules if they are to be marketed in the EU, or with US law for sale there.

In addition, Isle of Man rules relating to the employment of health care professionals, as well as medicines and medical devices are often modelled on UK standards, and so indirectly may import EU standards where applicable.

The Isle of Man Government introduced a smoking ban in public places one year later than the UK, which although not required under the terms of the Island's relationship with the EU, did meet EU rules on best practice.

Implications for the Isle of Man, if the UK leaves the EU, in respect of health and social care

In terms of the provision of health and social care, the UK leaving the EU would have little or no impact upon the Island's continued ability to provide these services for Isle of Man residents. Similarly, it would appear to be unlikely that this would affect the Island's ability to access tertiary health care services in the UK, which is subject to negotiation and contract between Isle of Man and UK health providers.

As noted in previous sections of this report, the Isle of Man must treat nationals of all EU Member States equally, and it is important to note, therefore, that under existing arrangements nationals of all Member States who qualify as 'ordinarily resident' would qualify for treatment, irrespective of their nationality (i.e. all EU nationals treated equally, provided they met the 'ordinarily resident' criteria). If Protocol 3 ceased to have effect, then this obligation would similarly fall away, but it must be noted that obligations to provide care under other international agreements, and bilateral treaties would remain.

The ability to employ health and social care professionals would continue to be dependent upon other factors (nationality and free movement) which are covered elsewhere in this report. As has been identified in respect of other economic sectors and service areas, free movement of people is important for the Isle of Man, as it is not able to produce or train the all of the specialists necessary to keep the Island functioning. It is therefore vital that free movement be retained between the Isle of Man and the UK – at least – and potentially, beyond into the wider EU.

As discussed above, other areas of EU competence which are followed as best practice, or standards which are adopted in order to access EU markets or facilities/services, would continue to apply to the Isle of Man in a similar manner – that is to say that they are not necessarily legally binding, but could continue to be followed on a voluntary basis.

8.e. – Treasury – Social Security

Each Isle of Man social security benefit has a condition requiring a person claiming the benefit to have spent some time in the Island before qualifying for the benefit.

Social Security Reciprocal Agreements with the United Kingdom

However, the reciprocal social security agreements between the Isle of Man and the UK provide, for example, that residence/presence in the UK may be treated as residence/presence in Isle of Man, and vice versa. This would usually allow a person moving between these countries to satisfy the residential requirements for, say, child benefit and universal disability benefits.

In relation to state pensions, up to 5th April 2016 this was more an administrative process whereby National Insurance Contributions were transferable between the Isle of Man and the UK which allowed people to draw their (consolidated) state pension entitlement in the country in which they lived during their retirement. However, for persons reaching state pension age on or after 6th April 2016 broadly speaking the state pension schemes of the Isle of Man and the UK will operate independently, with National Insurance contributions paid in the Isle of Man counting only towards state pensions in the Island and National Insurance contributions paid in the UK only counting towards the UK state pension; from April 2016 there will be no transfer of NI contributions between the countries and people with NI contributions in both countries will have to make separate claims for their IoM and UK state pensions.

The Agreements also provide that NI contributions paid in one country may count towards entitlement to bereavement benefits and short-term benefits (for example, contribution-based jobseeker's allowance, incapacity benefit and maternity allowance) in the other.

As regards child benefit a person claiming this benefit or the child for whom benefit is being claimed must have lived in the Isle of Man (or the UK by virtue of the reciprocal social security agreement with the UK) for at least half of the previous 52 weeks, or the child must have been born in the Isle of Man. But a person can be treated as having satisfied this condition if (for instance) the person claiming benefit starts work in the Island, pays National Insurance contributions and intends to stay in the Isle of Man for the following 6 months.

All persons claiming income-related benefits (e.g., income support) must satisfy an **"Isle of Man worker test"**, closely modelled on IOM control of employment legislation, to qualify for benefit, unless it would be "exceptionally harsh or oppressive" to deny them benefit. The social security agreements referred to above do not extend to income-related benefits. This test is almost the same as that under the Control of Employment Act 2014, but excludes persons who qualify as an Isle of Man worker under that Act because their spouse or civil partner is an Isle of Man worker by virtue of having received full-time education while they were ordinarily resident in the IOM.

Reciprocal social security agreements with other EEA countries

The Isle of Man is party to UK Social Security Agreements with EU and EEA Member States which pre-date the UK's accession to the EU. Although in respect of Member States these have been superseded by EU "co-ordination" rules, they continue to have effect for the Crown Dependencies. These agreements allow workers coming from abroad and Isle of Man residents going to work abroad to:

- avoid paying social security contributions in more than one country at the same time;
- aggregate social security contributions paid in different countries to qualify for social security benefits in another country (e.g., old age pensions);
- allow social security contributions paid in another country to count towards entitlement to short-term benefits (e.g., unemployment, sickness and maternity benefits).

Some agreements are more extensive than others. Agreements with EEA countries tend to cover more matters than those with other countries outside the EEA.

If the UK left the EU

If the UK left the EU, then the agreements described above, including those with the UK, would continue to have effect.

Similarly, access to income-related benefits would continue to be subject to an 'Isle of Man worker test' and would therefore similarly be unaffected by the UK leaving the EU.

As mentioned in other sections of this report, the 'equal treatment' Article of Protocol 3 would cease to have effect if the Protocol itself ceased to have effect. This might mean that the Isle of Man would be free to put in place rules which may be deemed to be discriminatory, in that they might distinguish between UK nationals and EU nationals for the purpose of access to social security or income-related benefits.

EEA nationals currently have a right of admission to the UK (and IoM) on producing a valid ID card/passport issued by an EEA state. If the UK left the EU, EEA nationals from outside the UK might become subject to immigration control, which is not currently the case. From a social security benefit perspective, section 150E of the Social Security Contributions and Benefits Act 1992 as it has effect in the Island currently provides that persons subject to immigration control are not eligible for most income-related or non-contributory benefits (however, there is no such exclusion from entitlement to contributory benefits). The [Social Security \(Immigration and Asylum\) Consequential Amendments Regulations 2000](#) provide a number of exceptions to rules excluding persons subject to immigration control from entitlement to some “publicly funded” social security benefits.

A “person subject to immigration control” is defined as a person who –

- (a) requires leave to enter or remain in the Isle of Man but does not have it;
- (b) has leave to enter or remain in the Isle of Man which is subject to a condition that he does not have recourse to public funds;
- (c) has leave to enter or remain in the Isle of Man given as a result of a maintenance undertaking; or
- (d) may not be removed from, or required to leave, from the IOM while appealing against an immigration decision.

Conclusion

Assuming there would be no changes to the current social security legislative provisions for EEA nationals, withdrawal from the EU would be unlikely to affect the manner in which the Isle of Man applies its social security provisions, or access to benefits for Isle of Man residents. Because the Isle of Man is not a part of the EU, it already restricts access to benefits – albeit in a manner which does not discriminate between EU nationals – in a way which might not be possible, if it were subject to EU rules.

8.f – Treasury – Direct taxation

Taxation remains primarily a competence of national governments rather than the EU. No businesses or private citizens pay tax directly to the EU and the main role of the EU on taxation policy is its efforts to align the tax systems of the member states to ensure a level playing field for businesses and to facilitate cross-border trade. This is especially relevant for those Member States within in the Eurozone.

A number of initiatives have, and may in the future, have an indirect impact on the Isle of Man, because although taxation matters sit outside of the scope of Protocol 3, the Island has opted to comply with certain EU tax provisions for practical and reputational reasons. This is aligned with the Isle of Man Government’s broader tax strategy, whereby it has taken the stance that it must adhere to prevailing global standards on tax and transparency in order to protect and enhance its reputation.

Building on the work originally undertaken in the OECD on harmful tax practices, the EU established the Code of Conduct Group (business taxation), which sought to identify and eliminate tax practices that could be deemed to be ‘harmful’ to competition across the Single

Market. The Code Group is a political arrangement between the Member States and the Isle of Man has voluntarily agreed to comply with the Code Group, and is represented within the Group by the United Kingdom.

In addition, the Isle of Man adopted and implemented the provisions of the EU Savings Directive, initially by applying withholding taxes and providing some information automatically, and subsequently moving to full automatic exchange of tax information. The EU Savings Directive has now been repealed and replaced within the EU by a new directive that effectively replicates the new global standard on automatic exchange of information, the Common Reporting Standard (CRS). The Isle of Man will not apply the new directive as such, rather, as the Isle of Man was an early adopter of the CRS, it will implement the CRS with EU member states in the same way as it is implementing the CRS with other countries. As the EU Savings Directive was implemented via 28 bilateral agreements a process is currently underway to suspend and then terminate these agreements.

Potential impact of UK exit on the Isle of Man

In the field of direct taxation a number of factors affect the manner and the extent to which international standards impact on the Island, and whilst the UK's existing and future relationship with the EU has a bearing in this area, it does not represent the full picture.

The EU is to a large degree aligned with the OECD's ongoing work on the elimination of harmful tax practices along with moves towards increased transparency, and also the recent work on Base Erosion and Profit Shifting. As in the field of financial regulation (of banking and other financial services) the work of many international forums is often codified and legislation produced at an EU level, depending on the respective competences of the EU and its Member States.

It is against this international/global agenda, therefore, that the relevance of EU tax legislation and co-operation must be set. As noted, above, the Isle of Man adopted and implemented the provisions of the EU Savings Directive, but this has now been repealed and replaced with the Common Reporting Standard (in addition to the US FATCA and UK FATCA style agreement) developed by the OECD and given effect by multilateral instruments that apply to many more countries than the 28 EU Member States. It is the case, therefore, that in relation to exchange of tax information, the relevant standard is not now an EU one.

It would be the case that the Isle of Man would no longer be subject to the strictures of the Code Group, as it is represented on that group by the UK, in its capacity as a Member State. It is likely, however, that the Code Group will be reinvigorated, amid calls from the European Parliament and the Council of the European Union that its remit be broadened. The European Commission, as well as the Code Group, is already investigating ways of classifying harmful tax practices in Third Countries, including the identification of 'tax havens', against which counter-veiling measures may be taken. It could be argued that this process, which may be potentially damaging to the Island's reputation, would continue whether the UK was a Member State or not and without the UK the Isle of Man would have no representation at all on bodies like the Code Group.

Conclusions

- The UK leaving the EU would not negate the need to comply with the majority of international tax standards upon which the EU's rules are based. Measures on tax transparency and the abolition of harmful tax practices – including measures to counteract the harmful effects of base erosion and profit shifting – would continue to be advanced by the OECD, as well as the EU, and the Isle of Man is likely to

participate in this work (at OECD level), and to meet those developing standards.

- The EU will continue to set its own rules, and the measures which must be adhered to in order to maintain access to EU markets will of course continue to be set by the EU itself. It is worth noting that Andorra, San Marino and Monaco (which are in the process of negotiating association agreements with the EU) have all signed tax co-operation agreements recently, as have Liechtenstein and Switzerland. The role of the EU's Code Group is likely to be expanded, and the Commission is set to re-examine the way in which it defines 'tax havens', as well as the counter-measures it may employ to penalise them, as well as companies which use them.
- The withdrawal of the UK from the EU would remove a strong voice in the Council which is opposed to deeper integration in the field of direct taxation – and this includes discussion of a potential harmonisation of effective tax rates – as well as a voice which can be employed to speak in support of the Crown Dependencies and Overseas Territories.

9. – Provision of Government services (Boards & Offices)

- a. Cabinet Office
- b. Her Majesty's Attorney General's Chambers
- c. General Registry
- d. Office of Fair Trading
- e. Data Protection
- f. Gambling Supervision
- g. Post Office
- h. Manx National Heritage
- i. Manx Utilities Authority
- j. Communications Commission
- k. Financial Services Authority (see section 7a. above, p.36, Financial Services)

9.a – Cabinet Office

9.b – Her Majesty's Attorney General's Chambers

9.c – General Registry

The exercise of the functions of Cabinet Office and Her Majesty's Attorney General's Chambers would be largely unaffected by UK withdrawal from the EU, as they are focussed on the delivery of services supporting other areas of Government. In respect of the Cabinet Office, this includes the support of the Chief Minister, Council of Ministers and Lieutenant Governor, as well as the provision of HR and IT for the rest of Government. Similarly, Her Majesty's Attorney General's Chambers provide legal services and advice for other Government Departments, as well as prosecuting criminal cases. The General Registry provides for the management of civil and land registries, as well as administrative support of the courts and legal aid services.

However, the impact of a UK withdrawal may well have significant impact on the workloads of the Cabinet Office and Her Majesty's Attorney General's Chambers in the sense that there would be considerable work required in Chambers to disentangle the current legal framework which underpins the Island's existing Protocol 3 relationship with the EU. Similarly, the Cabinet Office, which also encompasses the Isle of Man Government's External Relations function, and the Immigration, Passports and Nationality Service (see section 4) would also be required to undertake considerable work to assess and deal with the detailed

implications of the UK (and Isle of Man) withdrawal process, as well as supporting the process of renegotiation.

As UK withdrawal from the EU would have significant legal and constitutional implications, the impact in terms of workload could have a very significant impact on this area of Government.

9.d – Office of Fair Trading (OFT)

The OFT is responsible for the Island’s legislation in relation to trading standards, weights and measures and consumer protection. Whilst Protocol 3 does not, in general, apply EU law in these areas, at a practical level most goods supplied in the Isle of Man are produced to UK standards which are in themselves EU compliant. Whilst in theory the Island has freedom to not apply EU standards in these areas, it also needs to recognise the potential for technical rules to be construed as a restriction on trade in goods and thus engage Protocol 3.

Under Part 2 of Fair Trading Act 1996, the OFT is responsible for the Island’s competition law. Whilst Protocol 3 does not require the Island to apply EU competition law, there is again a requirement to ensure that anti-competitive practices do not become an artificial barrier to trade in goods; and thus breach Protocol 3. Part 2 of the Fair Trading Act 1996 provides a very basic framework of competition law.

It is also worthy of note that Isle of Man consumers and businesses derive indirect benefit from EU competition law in several ways:-

- Local consumers buy goods through a range of online channels which operate under EU laws;
- Local businesses have access to UK and EU markets;
- Many UK firms operate in the Island (either directly or through subsidiaries) and do so to the standards of their UK operation;
- Isle of Man markets derive indirect protection from EU competition law.

What if the UK withdraws from the EU?

Weights and Measures

The reality is that the vast majority of goods sold in the Island are imported from the UK and at a practical level, the Island has no real alternative but to follow whatever post-Brexit rules the UK introduces. It is common sense from an economic perspective that, as part of any free trade agreement, there would be measures to prevent artificial barriers to trade and that in turn requires the harmonisation of weights and measures.

Trading standards and consumer protection

At the present time the Island has the freedom to determine the extent of its trading standards and consumer protection framework; and has done so on a scale relevant to a small community. It is, nonetheless, influenced by UK legislation given that consumers themselves have expectations which are influenced by, for example, UK media. This is another area where it is possible to create (inadvertently or not) artificial barriers to trade. There is also a need to look at compatibility issues because local consumers trade via online and other mediums with the UK and EU. If there is a divergence of UK and EU standards following Brexit, there would need to be a review of Manx legislation. Certainly trying to maintain reasonable compatibility with both UK and EU standards would be much more difficult than at present, when UK standards are compliant with EU standards.

Competition

In the context of membership of the Single Euro Payments Area (SEPA), it was clear that the Island's competition law under Part 2 of Fair Trading Act 1996 falls far short of equivalence with Articles 101 and 102 of the Treaty on the Functioning of the European Union; hence the need for the Payment Services Act 2015. The OFT is proposing to introduce a new Competition Bill into the House of Keys following the 2016 General Election but even that, as currently instructed, falls short of equivalence with Articles 101 and 102. What we are trying to do is find a framework which meets modern standards but does not introduce unnecessary red tape, which will impact negatively on the economy. In other words, something that works on an Isle of Man scale. Interestingly, both Guernsey and Jersey have adopted a different approach and introduced amended UK legislation which, whilst closer to EU standards, has created its own expensive bureaucracy.

Conclusions

It is clear that any decision that the United Kingdom takes to leave the EU would create a short-term requirement for legislative change at a level and pace that is beyond the current capability of the OFT.

9.e – Data Protection

The Isle of Man Information Commissioner is responsible for the supervision and enforcement of the Island's Data Protection legislation.

The Isle of Man is among a small group of only 11 jurisdictions worldwide that have been officially assessed by the European Commission as having "adequate" data protection standards enshrined in domestic law, meaning that such standards are consistent with the EU's 1995 Data Protection Directive. This so called "adequacy decision" by the Commission allows for data to flow efficiently between the Isle of Man and the United Kingdom and other EU/EEA Member States, and is a vital component in ensuring the continued close economic ties with the UK.

Regardless of whether the United Kingdom votes to remain in or leave the EU, if the Island wants to be able to trade with the rest of the European Union and in doing so transfer personal data freely then it must continue to maintain the EU adequacy finding, as determined by the European Commission.

If the UK was to leave the EU and not become a member of the EEA, then for the same reason the UK would also have to seek an adequacy finding in order to transfer personal data between it and EU member states.

However, it should be noted that that Council of Europe Convention 108 also applies to the UK and was extended to the IOM in January 1993. Convention 108 is the original Data Protection instrument dating from January 1981 and in common with the EU Data Protection directive is in the process of being updated. It is expected that the revised Convention will be similar to the EU's new General Data Protection Regulation (GDPR). While the revised convention will have to be ratified, it is likely that the UK will do so.

From a practical perspective, if the UK were to leave the EU then how it seeks to implement the GDPR to obtain adequacy will be of importance. In theory the Island may be able to mirror the UK's legislation.

9.f – Gambling Supervision Commission

The [Gambling Supervision Commission](#) ('GSC') is an independent statutory board established in 1962. In addition to the licensing and regulation of land-based gambling operations (casino, amusement and slot machines, betting offices and lotteries), the Commission also regulates all online gambling activities, which have grown significantly in recent years. The core principles the Commission upholds are:

- to keep the gambling industry crime free.
- to protect the young and those at risk.
- to ensure that the services offered by licence holders are fair and that players receive their true winnings

In the event of the UK voting to leave the EU, it is unlikely that the areas of responsibility of the Commission would be impacted, given the Island's current position outside the EU.

The UK is the Isle of Man's conduit through which it can have some say on EU gambling matters. The relationship with the UK is good, and it has been very good at seeking input and sharing outcomes from the discussions and deliberations of the [EU Expert Group](#). This allows the Island, as well as the other Crown Dependencies and Gibraltar to put their comments to the UK who may represent them at the Expert Group meetings.

In addition, the Gambling Regulators European Forum (GREF) is a body comprising many European regulators. Whilst it was previously relatively EU-centric, with the help and support of the UK, it has become a much broader grouping of European regulators, including non-EU Member States and dependencies.

Whilst these illustrate a perhaps less tangible benefit for the Island of continued UK membership of the EU, they are perhaps indicative of the influence or soft-power which may be lost or diminished, should the UK vote to leave the EU.

9.g – Isle of Man Post Office

Royal Mail (RM) – it is unlikely the relationship between the Isle of Man Post Office (IOMPO) and Royal Mail (RM) would be impacted on by a UK exit. Royal Mail handles all aspects of the Island's relationships with international Posts and this is not foreseen as likely to change. IOMPO only has a commercial relationship with Royal Mail and not with individual international Posts. RM follows Universal Postal Union (UPU)/PostEurop criteria for commercial dealings with other countries or negotiate bi-lateral agreements and there is unlikely to be any impact in this arrangement for IOMPO.

Customs clearance – as noted elsewhere, there may be implications for Island trade if the free movement of goods was restricted. IOMPO works closely with Isle of Man Customs & Excise (IOMC&E) for the customs clearance of goods being imported to the Island from outside the EU. IOMC&E raises duty and tax on imported goods from outside the EU and this may need to be extended to EU countries. C&E already screen EU & non EU consignments for prohibited & counterfeit goods but the additional workload to C&E and IOMPO would increase. Non EU goods are generally delayed by at least one day for the clearance process so it is to be expected that there would be a similar increase in the delivery time if EU goods faced the same treatment affecting customer service standards accordingly. Goods exported from the IOM to EU countries may then require the same documentation as current non EU destinations. There is a global project running involving Posts and customs authorities to create an electronic pre-advice system for goods moving

internationally using the postal CN22/23 customs clearance system (this is the postal equivalent of general cargo customs clearance).

EU Postal Directive – the EU has issued a Directive (3 iterations) concerning postal services. IOM postal service and market is believed to be too small to be impacted on by the recommendations on competition and they have had no real domestic impact on IOMPO. EU exit does not offer any threats or opportunities in this respect.

VAT treatment - the EU legislated on the criteria for VAT to be applied to postal services and there was a high profile ECJ case (brought by TNT) about how VAT is applied in the UK which caused some changes in which services attract VAT and which are exempt. EU exit may give scope for the UK VAT rules to be changed.

IOMPO has joint membership with Jersey and Guernsey of PostEurop, and this will not change. The IOM is represented at the UPU, under a joint membership with the UK and other Crown Dependencies, by the UK (BIS¹⁰) – again, UK withdrawal from the EU would not affect this.

To conclude, the main potential impact of UK withdrawal from the UK would be likely to be the impact on the Island of any restrictions on the free movement of goods and any adverse change in the application of VAT to postal services.

9.h – Manx National Heritage

The EU has very little competence which directly affects the area of Culture and Heritage.

Access to EU funding has benefited some of Manx National Heritage's (MNH) museum and heritage partners in places like Liverpool, Orkney and Shetland significantly. For example, MNH work closely with the Shetland Amenity Trust and many areas of their work have benefited from EU programmes, including wild-life and biodiversity.

In addition, UK withdrawal from the EU could result in a significant impact in terms of many of the funding programmes for other purposes such as regional development and technological innovation which have culture and heritage outcomes. Many urban regeneration schemes are based on heritage areas or buildings. Increasingly, the EU is becoming involved in tourism – which again often features culture and heritage. As an example, MNH is currently an Associate partner in a project called "Follow the Vikings" which is funded under the Creative Europe programme. Although not eligible for funding, the Isle of Man benefits from being a partner.

An additional area of interest is the export of works of art and antiquity. The Manx Museum and National Trust has statutory authority to block the export of significant items from the Island. This is tied closely into Customs controls and is impacted by whether an item is likely to leave the EU.

9.i – Manx Utilities Authority

The Manx Utilities Authority (MUA) is responsible for providing its customers with safe, reliable, efficient and economic supplies of electricity, natural gas and clean water; as well as processing waste water, and delivering flood risk management services. In addition to operating a successful energy trading enterprise, Manx Utilities has two subsidiary

¹⁰ UK Department for Business, Innovation & Skills (BIS)

businesses specifically focussed on commercial telecommunications and subsea cable management.

In terms of the supply and generation of electricity side there should be little or no change to the situation in the Isle of Man as it connected as an embedded generator within the UK electricity market.

With relation to gas, if the UK left the EU, then the relationship between the UK and the EU will change; the UK would become a third country and the arrangements governing the interconnection points between the various jurisdictions (UK-Ireland, UK-Belgium and UK-Netherlands) would be revised. However, the UK will continue to be both an important hub for the delivery of Norwegian and UKCS gas (to the EU, and as the sole transit route for gas to Ireland) and a significant importer of gas from the EU. As such, it is difficult to imagine that anything will have a substantive impact on the transit of gas between Britain and the EU (Ireland).

It is not expected, therefore, that there would be any meaningful impact on security of supply for the Isle of Man if the UK left the EU. The changes are likely to be strictly technical and commercial. The costs of transporting gas to Ireland could increase, and so Isle of Man gas supply could also become more costly.

9.j – Communications Commission

The Communications Commission licences and regulates telecommunications and broadcasting in the Isle of Man.

The Commission works closely with OfCom in the UK, and the UK represents the Isle of Man at EU level as well as on a number of international bodies which regulate mainly technical aspects of spectrum management. Ofcom is directed by the UK Government to represent the UK at the European Conference of Postal and Telecommunications Administrations (CEPT), the Electronic Communications Committee (ECC), the Com-ITU and the Council of the European Radiocommunications Office (ERO).

As a Member State, the UK applies EU standards and rules in relation to telecoms, spectrum and TV broadcasting. These include the Radio Spectrum Policy Decision 676/2002/EC and Commission Decision 2002/622/EC (which establishes a Radio Spectrum Policy Group).

Due the Island's very close relationship with the UK in these areas, it is the case that many of these rules will be imported into the Island, in terms of technical standards. However, because the Isle of Man's Protocol 3 relationship with the EU does not extend to cover services – such as telecommunications – the commercial aspects of EU policy, such as provisions to reduce the cost of roaming charges, do not apply.

If the UK were to leave the UK however, it is unlikely that this position would alter significantly. The Isle of Man would continue to be classed as a Third Country, for commercial purposes, but it is likely that the UK would continue as a member of the relevant international bodies, and through the UK, the Island would be required to meet prevailing international standards.

10 – Alternatives to EU Membership

Numerous studies, position papers and opinion pieces have been published which set out the alternatives to EU membership, which could be negotiated by the UK, should it vote to leave the EU.

The UK Government published a paper entitled 'Alternatives to Membership – possible models for the United Kingdom outside the European Union'^[1], in March 2016, which sets out the following alternatives –

- The Norway model – in the European Economic Area (EEA) as a member of the European Free Trade Association (EFTA) but not in the EU
- Negotiated bilateral agreements, including –
 - The Swiss model – a series of bilateral agreements
 - The Turkish model – customs union
 - The Canadian model – A Free Trade Agreement
- World Trade Organisation (WTO) membership – reliance on WTO rules to set limits for trade barriers/tariffs

The UK Cabinet Office paper set out a detailed analysis of the advantages and disadvantages of each of the alternative models, and the UK Government position on these alternatives is outlined below.

The Norway model

The Norway model would give the UK considerable but not complete access to the Single Market. It would be outside the EU Customs Union, and would lose access to all of the EU's trade agreements with 53 other markets around the world. Re-negotiating these would take many years.

Norway is obliged to accept the free movement of people and has chosen to be part of the Schengen border-free area. In addition, Norway makes significant contributions to the EU and is subject to EU rules. If the UK negotiated EFTA membership, the UK would be bound by many of the EU's rules, but no longer have a vote or veto on the creation of those rules. (It is estimated that this could be up to 80% of EU legislation).

To adopt the Norway model, the UK would need the agreement of all the remaining 27 EU countries, along with Iceland, Liechtenstein, and Norway.

Negotiated bilateral agreements

The Swiss model

Switzerland has only partial access to the Single Market. It has most access to trade in goods. The bilateral agreements include various provisions to reduce practical barriers to cross-border trade. However, agriculture is not comprehensively covered by these agreements, so some agricultural products remain subject to tariffs.

[1]

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/504661/Alternatives_to_membership_possible_models_for_the_UK_outside_the_EU_Accessible.pdf

Switzerland has limited access to trade in services. The bilateral agreements only provide partial coverage, with only some sectors covered, such as some types of insurance and public procurement. But Switzerland has limited market access for professional services, including accountancy, auditing, and legal services. Relevant individuals, including self-employed professionals, can only provide services in the EU for a maximum of 90 days each year. This places significant constraints on Switzerland's capacity to export to the EU in these sectors.

Switzerland has no general access to the EU market in financial services. It is not part of the passporting system that minimises the regulatory, operational and legal barriers to the provision of financial services across the EU. Because Switzerland does not have a bilateral agreement with the EU on banking, Swiss banks need to establish a subsidiary in an EU/EEA country, such as the UK, in order to obtain financial services passporting rights. UK banks would need to do the same inside EU countries if the UK were to leave the EU.

Canada (Free Trade Agreement) model

Free Trade Agreements involve a more detached relationship with the EU. This means fewer obligations, but less access to the Single Market. Countries agree market access and tariff levels with the EU, and set quotas for trade between them. Exporters who wish to sell to the EU Single Market are required to comply with Single Market rules in the same way that exporters from Norway and Switzerland do.

The EU has trade agreements with 53 markets. These agreements provide varying levels of market access. For the EU, they are negotiated by the Commission, on behalf of the EU and its Member States. The agreement must then be approved by Member States, and the European Parliament.

The agreement between the EU and Canada goes further than any existing EU trade deal. Negotiations between the EU and Canada took seven years and were concluded in 2014. Before the agreement can enter into force, it must be approved by the EU (including the Council and the European Parliament).

Once it comes into force, the agreement provides for phasing out of all tariffs on industrial and most agricultural goods entering the EU. This deal addresses a number of other directly discriminatory measures such as quotas and subsidies for industrial goods.

Turkish model

Turkey has partial access to the EU Single Market. The arrangements cover industrial goods and processed agricultural goods, which means that customs checks are not required for these products. However, arrangements do not cover raw agricultural goods, or services. In areas where Turkey has access to the EU market, it is required to enforce rules that are equivalent to those in the EU. This includes competition, product, and environmental rules. Turkey is also required to align rules on State Aid (government support to businesses) with EU rules. The Agreement with Turkey provides some limited migration rights for Turkish nationals to reside in the EU.

General observations

Overall, the UK's assessment of negotiated bilateral agreements is that –

- A bespoke UK-EU trade agreement would be complex to negotiate. The EU-Canada agreement, for example, took seven years to negotiate and is still not in force. A UK-EU agreement would require the agreement of all 27 of the remaining EU Member States. The European Parliament would also need to give its approval.
- No existing bilateral trade agreement would deliver the same level of access that the UK currently enjoys to the EU Single Market. In particular, none provides equivalent access for services, which accounts for almost 80 per cent of the UK economy.
- Access to the Single Market would be linked to the obligations which the UK would be prepared to accept. A trade agreement such as that between the EU and Canada would bring less access to the EU market than the UK currently enjoys in, for instance, financial services, but would not require the UK to accept the free movement of people or make significant contributions to EU spending. Switzerland has more access to the Single Market, but has had to accept these obligations in return.
- The UK would lose the benefit of EU Free Trade Agreements with other parts of the world: renegotiating these would take years.
- The UK would lose its voice and vote over EU rules.

World Trade Organisation membership

In terms of any alternative relationship the UK may negotiate with the EU, WTO rules would represent a minimum threshold. It would be the most definitive break with the EU, offering no preferential access to the Single Market, no wider co-operation on crime or terrorism, no obligations for budgetary contributions or free movement of people.

If the UK did not manage to secure an agreement on better terms, it would be forced to revert to the WTO model. The UK Government states that this would cause a major economic shock to the UK, with serious consequences for companies, consumers, jobs and prices. They add that the UK would face immediate and heavy costs to its trading relationships, both with the EU and with the wider world. If reciprocal tariffs were introduced on imports from the EU, these goods would become more expensive.

In addition, UK nationals would not have the rights that they currently enjoy to live, work and travel freely in the EU. Under WTO rules, neither the UK nor the EU could offer each other better market access than that offered to all other WTO members.

The UK's existing privileged access to 53 markets outside the EU through the EU's Free Trade Agreements would be terminated. The UK could seek to negotiate new agreements, but this would potentially take years.

The implications and options for the Isle of Man

As covered in section 4 on constitutional and legal issues, the Isle of Man is not considered to be part of the metropolitan territory of the United Kingdom for the purposes of ratification and scope of international treaties entered into by the UK, and so any agreement reached by the UK with the EU would not automatically extend to cover the Island. In addition, the Isle of Man is not sovereign, and so it cannot enter into an agreement with the EU in its own right.

The effect of these two factors is to –

- firstly, give the Isle of Man a choice as to whether it agrees to inclusion within the scope of the UK's new relationship with the EU; and
- secondly, to limit the Island's own potential relationship with the EU, to either being the same as, or covering certain parts of, the UK relationship (subject to this being feasible and agreed by all parties). In other words, it is difficult to envisage how the Isle of Man could have a deeper or closer relationship with the EU, than does the UK.

This does, then, bring into focus the Island's options for its future relationship with the EU, which must be viewed in the context of the path which the UK itself chooses to follow.

The UK – Isle of Man relationship

As is discussed in the sections on free trade in goods, the free movement of people, and indeed, on the potential economic impact of UK withdrawal from the EU, it remains the case that the UK is the Island's most important trading partner, and that free movement of goods and people between the two would be of utmost importance. In addition, the Isle of Man is in currency union with the UK.

There is nothing to suggest that a Brexit would have an impact on the underlying constitutional relationship between the Isle of Man and the Crown/United Kingdom.

In addition, it is anticipated that the Customs and Excise Agreement with the UK, albeit in a potentially modified form, would continue, and the rights of Isle of Man residents to British citizenship would not be affected, should the UK leave the EU. The rights, however, of those British citizens to live and work in the EU, would be subject to negotiation.

The first priority, therefore, is to maintain the existing open trading relationship with the United Kingdom.

Alternative models

Each of the alternative models would have a different impact on the Isle of Man, as they may represent a broader or narrower relationship – and consequent set of responsibilities – than the Island's current relationship with the EU under Protocol 3.

These are assessed from an Isle of Man perspective below:

Norway model

If the UK joined EFTA, the Isle of Man would be in a similar position to what it was in when the UK joined (what is now) the EU. It would need to decide whether to be included in the UK's membership, whether it should stay essentially outside, or, whether to seek a compromise position, as it did with Protocol 3?

To enter EFTA with the UK, the Island would be required to accept the majority of the EU's *acquis communautaire* (or body of EU law), and this relationship would be far deeper than that currently enjoyed by the Island under Protocol 3. The Island would find itself in a position where a great deal of legislation adopted by the EU would be directly applicable in

the Isle of Man, but the Isle of Man Government would have no representation within the decision-making process, nor would the Manx people elect an MEP. In addition, Norway's relationship does not allow for inclusion within the Customs Union, nor for free trade in agricultural and fisheries products.

It can be assumed that the level of access to the Single Market which the Norway model would bring, however, would not come without certain conditions attached. The Island's tax regime may come under scrutiny, and there is a possibility that the Island would be required to contribute to EU funds if it was part of the EEA. The Island may also come under the jurisdiction of the EFTA court, which would seek to ensure relevant EU law was correctly applied in the Island.

Whilst it is not possible to be entirely certain how this option would affect the Isle of Man, it can be said that,

- Inclusion in the EEA requires the implementation of approximately 80% of EU law, without any chance of influencing how it is made
- There may be a requirement to contribute to the EU budget
- Some areas are not covered by the Norway model agreement – such as agriculture and fisheries

The UK Prime Minister has publicly rejected the possibility of the UK becoming a member of EFTA, and it would seem that the need to allow for free movement of people may be a barrier to the UK pursuing this option, if it were to vote to leave the EU.

Negotiated bilateral models

The Swiss model offers an 'a la carte' option, but it does have the disadvantage of being 'static' in nature, and so requires frequent updates and renegotiation, in order to keep up with EU developments. It may also present an attractive option for the Isle of Man, offering potential for free trade in goods, but it appears to be limited in terms of access for financial services. In addition, the EU is reported to be less than happy with the arrangements they currently have with the Swiss. Problems with the Swiss decision to restrict free movement of workers from the EU into Switzerland have meant that relations have been difficult.

The Turkish option would allow for participation in the Customs Union and limited free movement of people which is the arrangement which would most closely match that of the Island's current Protocol 3 relationship.

A Free Trade Agreement (FTA) may contain elements which would be beneficial to the Isle of Man, but the so-called modern FTAs are generally limited. Customs barriers would remain, and there would be no potential to benefit from the other FTAs which the EU has negotiated.

World Trade Organisation

As outlined in the UK position, this would represent the minimum relationship between the UK and the EU. The UK's membership of the WTO was extended to include the Isle of Man, but this status would require clarification if the Island were to rely on WTO rules to allow for trade with Europe.

Conclusion

The Isle of Man is not entirely free to choose what relationship it has with the EU. It may seek to benefit from all or part of the provisions negotiated by the UK, but at this stage, what those might be, is very far from clear.

In addition, it is also not clear what the EU might seek in terms of concessions from the UK or the Isle of Man. The EU is currently assessing how it might incorporate a requirement for third countries to meet its criteria for 'tax good governance' in order to access FTAs.

It would not be helpful, therefore, to suggest that the Isle of Man favours any one type of relationship ahead of any other, save to say that it would seek to ensure continued customs union with the UK, preserve VAT sharing arrangements (if the UK retains VAT, or similar tax) and to protect and potentially enhance the Island's ability to trade with the EU.

Useful next steps, in the period leading up to the Referendum will be to assess how the mechanics of renegotiation might be handled – and this would include how the Isle of Man might contribute to the process – as well as a discussion with the other Crown Dependencies, and the Devolved Administrations (see section 11 below), as to what their desired outcomes might be.

11 – Implications for the Devolved Administrations

Background

Prior to the announcement by the Prime Minister on the date of the referendum, the First Ministers of Scotland, Wales and Northern Ireland had argued against holding the EU referendum in June, noting it might distract from devolved elections taking place in May.

Nicola Sturgeon, Carwyn Jones and Arlene Foster wrote to the Prime Minister to urge him to defer the date, advising that a June date could "confuse" the process and make it hard to campaign effectively.

i. The Scottish Government

The Scottish Government has a long standing policy of support for European Union membership, both before and after the Scottish Independence Referendum. First Minister Nicola Sturgeon delivered a speech to the European Policy Centre¹¹ in Brussels in June 2015, setting out the Scottish Government's position on the EU In/Out referendum.

*"We understand and accept that the **result of the UK election** makes **a referendum inevitable**...and so I want to concentrate...on how the Scottish government can make a positive contribution to the process."*

On the possible constitutional consequences were Scotland to vote to remain, and the remainder of the United Kingdom favoured exit; the First Minister advised:

*"...if Scotland were to be taken **out** of Europe, despite voting as **a nation to have remained**, it would provoke a strong backlash among many ordinary voters in Scotland.*

¹¹ <http://news.scotland.gov.uk/Speeches-Briefings/First-Minister-speech-to-European-Policy-Centre-1977.aspx>

*Quite what the result of that would be, no one knows. But I have stated before that this could be one scenario producing the kind of **material change in circumstances** which would precipitate popular demand for a second independence referendum”.*

In November 2015, the Cabinet Secretary for Culture, Europe and External Affairs published a document entitled 'The Benefits of Scotland's EU Membership'¹² – this publication set out why the Scottish Government believes Scotland's EU membership should continue.

Cabinet Secretary Fiona Hyslop visited Dublin to give the keynote speech at the first meeting of the “National Conversation” established by the European Movement Ireland. The National Conversation sought to discuss the issues around the UK's European referendum and the potential implications for Ireland.

In a recent speech to the Resolution Foundation in London on the 29 February 2016¹³, the First Minister stated:

*“Let me be absolutely clear, I want the vote on the 23rd of June to result in **an overwhelming victory** across all parts of the UK **for remaining in the EU.**”*

*“If **less than two years** later (after the independence referendum) Scotland was to find itself **taken out of the European Union against our will**, because we had chosen to stay in the United Kingdom, it's **not hard to see why that might lead to a growing clamour for a further referendum.**”*

The First Minister has advised that she will actively campaign for continued membership in the run-up to June's referendum, “I believe that it's the **best outcome** for communities, businesses and individuals everywhere – across the European Union, and in all the **nations of these islands.**”

Having rejected independence in a vote in 2014, support for EU membership in Scotland remains higher than in other parts of the United Kingdom. Recent YouGov polls suggest that in the UK as a whole, 38% of people would vote to remain in the EU, 41% to leave and 21% were undecided. In Scotland 53%¹⁴ would vote to remain, 27% to leave and 20% were undecided. Scotland has been consistently more pro-European in successive polls.

ii. The Welsh Assembly Government

The Labour Government in Wales has an established pro-European position. Political opinion in the current National Assembly for Wales is broadly supportive of EU membership.

At the recent Welsh Labour Party Conference¹⁵, First Minister Carwyn Jones and Labour Leader Jeremy Corbyn warned about the impact leaving the union could have on businesses and the economy in the region. The Labour leader said that large numbers of jobs in North East Wales - over 121,000 across Wales - including those at Airbus in Flintshire, depended on trade with Europe. He also warned that important infrastructure investment for roads and railways came from the EU.

¹² <http://www.gov.scot/Resource/0048/00488952.pdf>

¹³ <http://news.scotland.gov.uk/Speeches-Briefings/Resolution-Foundation-2330.aspx>

¹⁴ Cited in speech by the Cabinet Secretary for Culture, Europe and External Affairs, 9 November 2015, Dublin

<http://news.scotland.gov.uk/Speeches-Briefings/Scotland-s-Future-in-the-EU-1f34.aspx>

¹⁵ <http://www.welshlabour.org.uk/events/2016/02/19/welsh-labour-conference-2016/>

Labour Member of the European Parliament, Derek Vaughan, has stated: "Outside the EU we would not get EU funding, for example all of the programs in the EU pipeline would stop¹⁶". On farming subsidies, he added "over 121,000 jobs and business depended on the relationship and if the nation voted to go Wales would be much worse off¹⁷".

The Welsh Government has long placed importance on maintaining good relations with the European Union. Back in May 2012, the First Minister launched '*Wales and the European Union – The Welsh Government's EU Strategy*¹⁸', this document outlined a strategy for increasing Welsh influence in the European institutions. Alongside this, the Welsh Government maintains a Brussels Office¹⁹ and representative in the European quarter.

Wales has, to-date, been the recipient of significant European structural funding, between 2014–2020, the Welsh Government has stated Wales will benefit from around £1.8bn²⁰ of European Structural Fund investment. A recent example includes a new £136m²¹ EU-backed fund to give businesses in Wales "access to finance to help drive their productivity and the growth of the Welsh economy" as announced by the First Minister.

Wales has historically been perceived as pro-European, however, according to recent reports, opinions could well be changing. UKIP is predicted to win as many as nine of the Welsh National Assembly's 60 seats in the Welsh elections in May 2016 "amid a growing tide of Euroscepticism²²". If this occurs, this will give a Eurosceptic party nearly as many seats as Plaid Cymru (Welsh Nationalists) currently hold.

Nonetheless, according to recent polling, the west Wales area of Ceredigion remains the most pro-European place in the UK²³.

In the event of a British exit from the European Union, it is considered feasible to suggest there would be a significant loss of EU funding to Wales resulting in a shortfall in Welsh Government income streams in the short to medium term. In the absence of a significant pro-independence movement advocating self-sufficiency, responsibility for managing an economic transition would theoretically fall to HM Government, in cooperation with the Secretary of State for Wales and the devolved institutions.

iii. **The Northern Ireland Executive**

The Northern Ireland Executive is a power-sharing Executive. As such, the two main parties have divergent views on EU membership. First Minister Arlene Foster and the Democratic Unionist Party (DUP) have confirmed they will campaign for Brexit²⁴ in the upcoming

¹⁶ *Six things Llandudno conference has revealed about Welsh Labour*, 21 February 2016

<http://www.dailypost.co.uk/news/north-wales-news/six-things-llandudno-conference-revealed-10924292>

¹⁷ *Ibid*

¹⁸ <http://gov.wales/docs/caecd/publications/120531eustrategyfinalmay12.pdf>

¹⁹ <http://www.wales.com/business/overseas-offices/european-office>

²⁰ <http://gov.wales/funding/eu-funds/2014-2020/?lang=en>

²¹ <http://gov.wales/newsroom/firstminister/2016/10941033/?lang=en>

²² <http://www.walesonline.co.uk/news/politics/ukip-course-win-nine-ams-10892548>

²³ <http://www.walesonline.co.uk/news/politics/part-rural-wales-most-pro-10967427>

²⁴ <http://www.belfasttelegraph.co.uk/news/northern-ireland/dup-confirms-it-will-campaign-for-brexit-in-leaveremain-referendum-34470806.html>

referendum. Mrs Foster has stated individual members of her party would be free to take opposing sides in the debate, but considers that the DUP has "always been Eurosceptic in its outlook". The DUP join the Secretary of State for Northern Ireland, Theresa Villiers MP in campaigning for a leave vote.

The other three parties in the Stormont Executive - Sinn Fein, the SDLP and the Alliance party - all support the UK staying within the European Union. Deputy First Minister Martin McGuinness has said the implications of a UK withdrawal from the European Union would be "absolutely enormous"²⁵ for Northern Ireland. Mr McGuinness questioned how a withdrawal would affect agreements made during the peace process:

*"Anybody that has examined our relationship in the north with the EU over the course of many years can't fail to recognise **enormous benefits** there have been for the community and voluntary sector, farmers and business community.*

*"I believe that right across the community - unionist and the broad nationalist/republican community - the majority of people place **great value on our membership of the European Union** and they want that to continue.*

Separately, the Ulster Unionist Party (UUP) has declared itself on the remain side of the EU referendum debate²⁶.

Were the United Kingdom to leave the European Union, hypothetically, this could cause a revisiting of sections of the Good Friday Agreement – particularly in relation to areas of close cooperation and travel arrangements between the Republic and Northern Ireland. It could be considered that this presents a risk to the existing political status quo.

In a UK Cabinet Office report on the consequences of leaving the EU, it was advised that the future of the Common Travel Area could be in doubt.

*"Northern Ireland would be confronted with difficult issues about the relationship with Ireland. Outside the EU's customs union, it **would be necessary to impose customs checks on the movement of goods across the border**. Questions would also need to be answered about the common travel area which covers the movement of people"²⁷*

However the Mayor of London Boris Johnson has questioned this view, arguing that Brexit would not affect Northern Ireland harder than other parts of UK²⁸. Additionally, the Secretary of State for Northern Ireland has told Irish media²⁹ that the common travel area between Ireland and the UK *can* viably continue – even if the latter votes to pull out of the EU. In common with the other devolved nations, the Northern Ireland Executive also maintains a Brussels Office and representation; assisting the Northern Ireland Executive to

²⁵ <http://www.bbc.co.uk/news/uk-northern-ireland-politics-35629360>

²⁶ <http://www.belfasttelegraph.co.uk/news/northern-ireland/ulster-unionist-party-supports-staying-in-eu-34514128.html>

²⁷

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/503908/54538_EU_Series_No2_Accessible.pdf

²⁸ <http://www.belfasttelegraph.co.uk/business/news/boris-johnson-brexit-wont-hit-northern-ireland-harder-than-other-parts-of-uk-34498868.html>

²⁹

<http://www.independent.ie/business/irish/travel-link-would-stay-if-uk-left-the-eu-villiers-34500627.html>

“further the aims of its Programme for Government through supporting Northern Ireland’s engagement with the EU³⁰”.

12 – Conclusions and next steps

It is clear that although the Isle of Man is not included within the UK’s membership of the EU, any change in the UK’s relationship with the EU, and whether it continues to be a Member State, will have a potential impact on the Island.

It is difficult to be certain what effect the UK leaving the EU would have on the Island, until the exact nature and scope of the UK’s new relationship is better known.

The referendum will take place on 23rd June 2016, and in the period leading up to this the Isle of Man Government will:

- Use this first interim report as the basis for further political engagement and discussions with UK officials on the mechanics of the negotiations, setting out the Isle of Man’s position;
- Hold discussions with the other Crown Dependencies, to understand their respective positions,
- Give further consideration as to the impact of Brexit on local business, as well as the potential effects of each of the models for the UK’s possible new relationship with the EU, should it vote to leave.

³⁰ <http://brusselsni.com/about/>



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