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NEWS ANALYSIS

Brexit and Tax Planning

by Lee A. Sheppard

The big news out of Blighty is that Manchester City have been banned from Champions League for the next two seasons for violating UEFA's financial fair play rules, which say clubs can't spend more than they earn. The club is majority owned by the Abu Dhabi United Group, the investment vehicle owned by Sheikh Mansour bin Zayed Al Nahyan. The Sky Blues were suspected of spending vastly more than they earned for some time, but no one seriously expected UEFA to act. UEFA said the subsidies were disguised as related-party sponsorships. The club is also accused of misstating its books and failing to cooperate in the investigation. If the penalties stick — the club will appeal — it could mean the unraveling of an empire carefully built over many years.

That empire revolves around manager Pep Guardiola, who has a year left on his contract. The whole club and management structure were rebuilt to his liking — even though he has a habit of fleeing clubs after a short tenure. The caliber of players the club attracts and retains will be seriously dented by the lack of Champions League football. Some stars have been promised seven-figure bonuses for Champions League qualification, which would come out of tournament revenues. To them, the Premier League and rituals like the FA Cup and the Manchester derby are meaningless. Ironically, local rivals Manchester United would see their chances of European football next season improved by the Manchester City ban. The Sky Blues' empire also includes feeder teams like New York City FC of the MLS (which has its own set of tight spending rules).

Could the Manchester City penalties be retaliation for Brexit? We can't possibly imagine. It's completely unfathomable that a European soccer governing body would punish a Premier League team. "Ultimately based on our experience and our perception, this seems to be less about justice and more about politics," Sky Blues CEO Ferran Soriano told the press. Interesting data point: Big-spending Paris Saint-Germain also have an Arab sugar daddy, Qatar Sports Investments (QSI), a Qatari government investment company, and have been accused of using a related-party sponsorship to breach financial fair play rules.

Um, why does U.K. Prime Minister Boris Johnson need to reshuffle his Cabinet so soon after he won office? Some members were Theresa May holdovers. And in a parliamentary system, Cabinet secretaries are often independent actors with their own power bases. Chancellor of the Exchequer Sajid Javid was either fired or resigned, which is the big news for our purposes. Javid's departure was prompted by a vicious argument with Johnson *consigliere* Dominic Cummings, who replaced HM Treasury advisers drafting the upcoming budget. That means the prime minister's office will assert more control over the Treasury function. Javid's 39-year-old deputy, Rishi Sunak, will replace him. That's right, readers, a millennial former Goldman Sachs employee now holds the second most powerful job in the British government.

This move is understood not so much as a strike against Javid's independence as it is against entrenched Treasury bureaucrats and their unwillingness to spend. Britain runs balanced budgets, and the Treasury civil servants think spending is a sin. Sunak is an advocate of freeports — tax- and tariff-free entrepôts like Switzerland has. The EU can be expected to object vigorously. Cummings has vowed to reform Whitehall — British vernacular for the permanent bureaucracy, which carries on pretty much the same way no matter which party is in power. Another Cummings target is the hefty mandatory license fee that finances Auntie Beeb, which has taken to lecturing the populace on political correctness.

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Manchester City's Kevin De Bruyne, possibly the world's best attacking midfielder. (Tim Goode/ZUMA Press/ Newscom)

Johnson's chief Brexit negotiator is David "Frosty" Frost (not the late talk show host), the former head of the Scotch Whisky Association, who studied medieval history at college. Frost argues that the United Kingdom should not have to adhere to EU rules any more than the Japanese do. Thierry Breton, EU single market commissioner, responded that the British helped write many of those rules. "They know that if they want to continue to benefit from what these rules have created, in other words, the largest single market, they know how to behave," he told the *Financial Times*.

While the official EU position is that the British must stay on EU rules temporarily and have equivalent rules thereafter, the French argue that the United Kingdom must promise never to diverge from EU rules (*Financial Times*, Feb. 16, 2020). A revised version of the official EU negotiating position moves closer to the French approach. The return of the Parthenon friezes to Greece may be added as a sensitive issue (*Financial Times*, Feb. 18, 2020).

As this article was being written, Frosty told his EU counterparts that the British would never agree to EU oversight of rulemaking in exchange for a trade deal. "To think that we might accept EU supervision on so-called level playing field issues simply fails to see the point of what we are doing," he said in Brussels. "It isn't a simple negotiating position which might move under pressure — it is the point of the whole project." The French insist that they are arguing not out of spite but — wait for it — concern for the environment (*Financial Times*, Feb. 17, 2020).

One Brexit fantasy is an advantageous trade deal with the United States, which takes a small proportion of British exports. President Trump, whose mother was a Scot, is an Anglophile and a friend of chief instigator Nigel Farage. But the Trump and Johnson administrations are having some disagreements. Michael Gove, minister for the U.K. Cabinet Office, scolded the Trump administration on environmentalism. And more seriously, Johnson decided to allow Huawei to build out the British 5G network. The U.S. government warned that Five Eyes intelligence sharing was at risk, and even Farage called that move a mistake. Chinese help is also being sought on infrastructure. Johnson has canceled previously scheduled trips to the U.S. capital.

Oh, but won't the British muddle through, like they always do? Falling out of the EU does not guarantee that WTO rules would apply. The United Kingdom would have to separately qualify for the WTO, of which it is currently a member through the EU. Auto parts — a big British export to the EU — are exempt from WTO tariff caps, which means they would be subject to full tariffs without an EU deal.

More to the point, the British can't feed themselves, despite a huge amount of the countryside having been turned over to industrial farming since World War II. British farming is subsidized through the EU's notorious farm policy and is uneconomic without the subsidies, which account for roughly a third of gross receipts. Some 80 percent of food imports come from the EU.

What's this got to do with taxes? Around here, we seem to talk about everything Brexit but taxes because when you can't do wholesale banking in the EU, taxes are not your biggest problem. But

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there are incipient tax problems, mostly caused by drafting international agreements as if no country would ever leave the EU. These were the subject of discussion at the February 18 International Tax Institute luncheon in New York. Mark Stone of Holland & Knight discussed U.S. treaties and Vincent van der Lans of Loyens & Loeff discussed EU directives.

Are the EU negotiators even thinking about tax problems? Big picture, yes. Technical issues of concern to our readers and discussed at the International Tax Institute, no. As the withdrawal agreement indicated, Europeans are anxious that the British not use tax law to extend state aid to companies and that Britain not become a tax haven. Europeans want the British to abide by the EU code of conduct on business taxation.

U.S.Treaties

A short history lesson. Americans come to treaty negotiations with a couple of basic demands: no withholding on outbound payments and no treaty shopping unless it's an approved shopper. But for the Netherlands, a treaty network is an essential feature of its corporate tax haven, and the U.S. treaty is the crown jewel of that network. So the Dutch came to the negotiations with their demands, which were rooted in EU law and interpretations by the Court of Justice of the European Union.

So in 1992, the Dutch asked the Americans to extend derivative benefits to all EU members. They had a sound legal basis for this request, which later took the form of the CJEU *Open Skies* cases (*Open Skies* (C-466/98, C-467/98, C-468/98, C-469/98, C-470/98, C-471/98, C-472/98, C-475/98, and C-476/98)). Those cases, which were brought by the European Commission, held that the nationality requirements of bilateral air transport treaties violated freedom of establishment under the Treaty on the Functioning of the European Union. The commission has made noises about forcing this theory onto bilateral tax treaties (MEMO/15/6006). (Prior analysis: *Tax Notes Int'l*, July 5, 2004, p. 45.)

U.S. negotiators worry about treaty shopping and inversions, so the United States has different treaties with different EU members. But the Dutch derivative benefits clause anticipates greater consistency in European tax and treaty policy in the long run. At one point, the commission asked U.S. negotiators to sign a treaty with the EU but Treasury refused on the view that the EU could not speak for its member governments. The CJEU has recognized that treaties are a member competence, so that taxpayers cannot argue for most favored nation treatment (*D* case, C-376/03). (Prior analysis: *Tax Notes*, July 18, 2005, p. 282.)

The concept of equivalent beneficiaries was introduced in the 1992 Netherlands-U.S. treaty. Under the derivative benefits test of the limitation on benefits article, the recipients of deductible payments also must be "equivalent beneficiaries" — that is, persons who would be eligible for treaty benefits themselves.

For a nonpublic company to have derivative benefits, it must be 95 percent owned by seven or fewer equivalent beneficiaries, which are defined as North American Free Trade Agreement- and EU-area residents that could otherwise claim comprehensive treaty benefits on their own on the basis of a NAFTA or EU member treaty with either the Netherlands or the United States. There is a base erosion test. Additionally, for an item of passive income, the NAFTA- and EU-area residents must show that they are entitled to treaty rates on passive types of income at least as low as those offered by the Dutch treaty (article 26(8)(f)).

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The equivalent benefits requirement is illustrated by an example in the Treasury explanation. A U.S. company is wholly owned by a Dutch company that is wholly owned by an Italian parent. Although the Dutch company would be exempt from U.S. dividend withholding, the Italian company would be eligible only for a reduced 5 percent rate under the Italy-U.S. treaty. That means the Italian parent would not be an equivalent beneficiary entitled to use the derivative benefits provision. The example focuses on the rate differential; both companies are EU residents.

Some 15 subsequent U.S. treaties and protocols were drafted this way. Coupled with the

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base erosion provisions of those treaties, a taxpayer could freely base erode within the EU, but not by shifting income from the EU to third countries, Stone pointed out. The equivalent beneficiary provision has a base erosion test that is different from the general base erosion test of the LOB articles of these treaties.

Stone gave the example of a French company with no active business that is owned by French and British investors. The company owns patents and collects royalties from U.S. licensees. It is ineligible for withholding relief on royalties under the France-U.S. treaty because it has no active business. While the United Kingdom was in the EU, the company was eligible for derivative benefits because it was owned by equivalent beneficiaries. With the United Kingdom out of the EU, the company is not eligible for withholding relief. But the British treaty provides withholding relief! The way these 16 treaties are drafted, equivalence is measured only by EU membership and not by the benefits available under a comparable treaty.

Stone's example highlights another feature of U.S. LOB articles — the active business exception. If the French IP company had an active business and the income at issue were derived from that business, then it would be entitled to treaty relief regardless of whether it's a qualified person. Holding companies, investment companies, and group finance companies are not considered to have a trade or business (article 22(3)).

U.S. negotiators know how to draft for equivalence based solely on comparable treaty provisions. Gibson, Dunn & Crutcher LLP lawyers pointed out that subsequent LOB articles have no geographic limitations on equivalent beneficiary status. But insofar as the EU treaties are concerned, a plain text reading of the equivalent beneficiary provision requires a conclusion of British ineligibility. For this the lawyers cite the Vienna convention on the law of treaties, which the United States has signed but not ratified.

The Canada-U.S. treaty, most recently amended in 2007, is drafted to permit use by equivalent beneficiaries eligible for equivalent treaties, regardless of where they are resident. The simpler equivalent beneficiary clause in that treaty entitles a company to the benefits of the dividends and interest articles if it is 50 percent owned by qualified persons and is resident of a country with which the other contracting state has a double tax convention, to which it is entitled to full benefits. The company is allowed to piggyback on its active business in that other country and must be entitled to a withholding rate at least as low as the Canada-U.S. treaty (article 29A(4)).

The 2016 U.S. model treaty takes the same approach as the Canada-U.S. treaty, so it would permit equivalent benefits for a resident of any country that can show it's entitled to the benefits of an equivalent treaty. That is, equivalence would be tested on the basis of treaty equivalence, not geographic proximity or membership in a trade bloc. Under the model, an equivalent beneficiary would be "a resident of any state, provided that . . . the resident is entitled to all the benefits of a comprehensive convention for the avoidance of double taxation between that state and the contracting state from which the benefits of this convention are sought . . . provided that, if such convention does not contain a comprehensive limitation on benefits article, the resident would be entitled to the benefits of this convention by reason of" being 50 percent owned by residents of either party (article 22(7)(e)(i)).

Is the EU equivalent beneficiary problem overstated? The EU officially told other countries to treat the United Kingdom as though it were still a member of the EU for the transition period. The European Commission put a diplomatic note on its website to notify 160 countries with which it has international agreements that the United Kingdom should continue to be treated as an EU member for a standstill period. The *note verbale* says that "the United Kingdom is treated as a Member State of the Union and of Euratom for the purposes of these international agreements" for the remainder of 2020. The Netherlands has stated that it will treat the United Kingdom as an EU member during the transition period.

The treaty dilemma is predicated on the assumption that some EU member government in the payment chain would object to a U.S. government decision not to withhold on outbound payments to a British ultimate payee. Really, when the intermediary companies are usually in friendly EU tax havens? The

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Luxembourg-U.S. treaty has an equivalent beneficiary definition that is keyed to EU membership (article 24(d)). If a U.S. company is paying dividends, interest, or royalties to an inactive Luxembourg company that is ultimately owned by British and French investors, the government that would be interpreting the Luxembourg treaty and making the decision about treaty eligibility for the payments is the U.S. government.

What other government is going to object to a permissive U.S. interpretation of a contract that is intended to grease the wheels of commerce? Is the U.S. government really going to sandbag the British investors because of some hyperliteral nitpicking about whether the United Kingdom is legally but not substantively out of the EU?

That seems unlikely. U.S. treaty interpretation is notoriously static — weirdly so, given that the United States is a large country whose treaties are intended to help smooth international business. U.S. treaty interpretation is frozen at the point when the treaty was signed. Was the United Kingdom a member of the EU when all 16 treaties were signed? Yes. Then it's meant to be covered, now and forevermore.

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A static interpretation also aligns with a contractual view of treaties (see *BG Group PLC v. Republic of Argentina*, 572 U.S. 25 (2014)). But this interpretive approach is most relevant to subsequent changes in the rules, not the facts (see *National Westminster Bank PLC v. United States*, 512 F.3d 1347 (Fed. Cir. 2008)).

Or is an equivalent beneficiary meant to be ambulatory? The drafters wanted to accommodate changes in facts, that is, EU membership or treaty status. Stone pointed out that Treasury's nonbinding technical explanation for the 1992 Dutch treaty explicitly calls for ambulatory interpretation. Regarding paragraph 8(h), the treaty definition of EU member, the explanation says that although Portugal had no U.S. treaty when the Dutch treaty was signed, Portuguese residents could in the future become equivalent beneficiaries if the United States and Portugal made a treaty.

Implying that the United Kingdom would fall out of equivalent beneficiary eligibility upon Brexit, the explanation states:

> This definition is ambulatory; if both States and Portugal conclude a comprehensive income tax convention, Portugal would be included within the definition. Conversely, if one of the Contracting States terminated its convention with a particular member of the EC or a member of the EC removed itself from the EC, that state would no longer be considered a member state of the European Communities for purposes of the Convention.

Treasury seems to concur with the ambulatory view. Treasury's view is that the EU reference involved certain commitments and was the subject of negotiation. When the facts change, treaty coverage changes. The 16 treaties technically require EU membership for equivalent beneficiary. The United Kingdom is out of the EU, which would mean that some British entities and investors have a real problem qualifying for derivative benefits.

"This is a change in facts. The United Kingdom used to be part of the EU, now it's not. I don't think it's crazy to say that, under the terms of the treaties, non-U.K. subsidiaries of U.K. parent companies no longer get benefits automatically," said former treaty negotiator Patricia A. Brown, director of the Graduate Program in Taxation at the University of Miami School of Law.

Treasury appears to be leaving application of the equivalent beneficiary definition for British entities up to the competent authority treaty assistance and interpretation team at the IRS. All derivative benefits provisions permit appeal to competent authority if relief was denied. Competent authority is seen as strict, so taxpayers don't want to go there. The process was intended as a safety valve from strict LOB rules.

"It's a little crazy to leave that to individual determinations by the competent authority,"

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Brown said. "It would be much better for everybody if the government put out a notice saying that entities in that situation that qualified under derivative benefits before would continue to qualify because clearly the company didn't plan into Brexit as a tax avoidance strategy."

Wouldn't most multinationals with affiliates affected by these treaties qualify for equivalent beneficiary status because they are publicly traded? Also eligible as equivalent beneficiaries are publicly traded companies, regardless of whether they would be entitled to the same treaty benefit claimed by the payee company. Stone and van der Lans explained that a British company could fall out of the public trading criterion, which is based on where shares trade, not volume.

Indeed, Steris PLC, which traded on the London Stock Exchange, was concerned. It had a U.S. operating company that paid interest to a Luxembourg group finance company — this is a standard setup for a European parent that doesn't have to worry about subpart F. Steris worried that it wasn't an equivalent beneficiary under the Luxembourg treaty, so it redomiciled to Ireland. Van der Lans pointed out that Steris had previously inverted out of the United States, so maybe it is especially tax sensitive.

Stone raised a question whether a British investor in a British company could be considered an equivalent beneficiary under the U.K.-U.S. treaty. The EU resident requirement is doubled up in that treaty. The pertinent provision states that an equivalent beneficiary is a resident of a member state of the EU or European Economic Area, but only if it would be entitled to all the benefits of a comprehensive double tax convention between any EU or EEA member from which the benefits are claimed, unless it lacks an LOB article (article 23(7)(d)).

So what this says is that for a British investor, the British treaty is not a good enough equivalent treaty! The Treasury technical explanation, which is not binding, states that qualified persons who are U.S. or U.K. residents are equivalent beneficiaries. Stone pointed out that a literal post-Brexit reading of the provision would lead to the opposite conclusion.

NAFTA treaties suffer from a similar drafting problem with the signing of the United States-Mexico-Canada Agreement (USMCA), but Treasury apparently does not see this as a problem because USMCA membership is not different. As Stone noted, USMCA just tinkers with NAFTA and has been oversold. But Treasury's interpretation of its international agreements is not constrained by extravagant public statements by the executive. Canada's lower house has passed the USMCA, and its upper house is expected to do so shortly. Then the USMCA will take effect three months later.

Why doesn't Treasury put out notices? Stone and van der Lans pointed out that there is precedent for notices. When the Soviet Union broke up, Treasury said its constituent parts should be treated as covered by the USSR treaty (Treasury News NB-1763). And when the British lease on Hong Kong expired, Treasury said it was not covered by the China-U.S. treaty (Notice 97-40, 1997-2 C.B. 287).

EU Directives

It's impossible to create Singapore on the Thames if inbound payments are subject to withholding at European borders. Van der Lans explained that European countries are likely to withhold on payments to Britain unless their bilateral treaties prohibit it. Readers might be surprised how many treaties have positive withholding, albeit at reduced rates. Many EU member countries' British treaties have 15 percent withholding on portfolio dividends and 10 percent withholding on interest and royalties. Outbound payments aren't a problem; the United Kingdom statutorily has zero withholding on dividends.

Now, multinationals can't even tolerate withholding at low treaty rates — hence the double Irish structure of yore. Yet, as van der Lans explained, some important European markets like Germany and anxious EU newcomers like Poland don't provide for zero withholding on some items. France has zero withholding in its British treaties. But Luxembourg's British treaties provide for 5 percent withholding on dividends and royalties. Ireland also has 5 percent withholding on dividends in its British treaty.

EU directives remove cross-border withholding taxes and other impediments in situations that are important to multinationals. The merger directive, 2011/35/EU, removes tax

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obstacles to cross-border mergers and protects creditors of the parties. Tax losses are transferable, but a merger has to have a business purpose (*Foggia-Sociedade Gestora de Participações Sociais* (C-126/10)). Most European countries still maintain exit taxes, which are constrained but permitted (*National Grid Industries* (C-371/10)).

Planners are reconsidering the Netherlands and Luxembourg for holding companies on the view that withholding on payments to the United Kingdom may be reinstituted. The parent-subsidiary directive, 2011/96/EU, prohibits withholding on dividends paid by EU subsidiaries to EU parents. It requires zero withholding for holdings of at least 10 percent of capital or voting power, so it covers large portfolio holdings as well. It was amended to deny a participation exemption for deductible payments (2014/86/EU). This directive makes EU holding companies possible.

Combined filing enables groups to use losses incurred elsewhere in the EU. The CJEU has held that combined filing cannot be restricted to domestic members or to groups that lack resident parents or subparents (some systems, like the German one, push everything up to the parent, which is the filer). But, as van der Lans explained, those CJEU decisions hinge on the presence of an EU resident parent. If a U.K.-parented group has to have an EU subparent for access to combined filing, that may make U.K. holding companies unattractive (*SCA Group Holding BV* C-39/13, C-40/13, C-41/13).

The interest and royalties directive, 2003/49/EC, enables income stripping by multinationals operating in Europe. The newly installed British patent box and the country's indulgence of group finance companies would be worthless if EU-source interest and royalty payments suffered withholding. On top of EU mandatory interest barrier rules, it would be very inconvenient for multinationals' supply chains if withholding interrupted these flows.

Then there's the anti-tax-avoidance directive, 2016/1164/EU, amended by 2017/952/EU, which came into full flower after the Brexit vote. It requires implementation of simpler European approaches to the BEPS recommendations. The British were enthusiastically implementing some of the BEPS recommendations even before the commission got around to imposing them. The United Kingdom was the first jurisdiction to enact the full platter of BEPS anti-hybrid rules. But British CFC rules are being criticized for being too indulgent of group finance subsidiaries (*Babcock International Group v. European Commission*, T-485/19).

The United Kingdom will implement DAC6, 2018/822/EU. Planners are unnerved by this prospect, but the United Kingdom being out of the EU won't make much difference in this realm. Britain itself has had tax scheme disclosure requirements for years. DAC6, however, requires reporting if a deductible payment is made to a resident of an EU blacklist country, which the Caymans just became (discussed below).

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The United Kingdom recently enacted the Criminal Finances Act, a nasty set of entity-level strict liability criminal penalties for enablers to tax evasion (whether U.K. incorporated, pursuing a U.K. trade or business, or acting in the United Kingdom). Criminal penalties attach to entity failure to prevent facilitation of tax evasion under British law or entity failure to prevent facilitation of tax evasion under the laws of any other country that defines evasion similarly to British law. So if a U.S. law firm with a British office failed to prevent facilitation of a tax crime in Brazil, there could be strict liability in the United Kingdom. (Prior analysis: *Tax Notes Int'l*, Apr. 10, 2017, p. 101.)

On the financial side, the British are suspicious that the Europeans could make changes to the markets in financial instruments directive (MIFID II), deliberately aimed at weakening London-based banks competitively. MIFID II (2014/65/EU) allows EU branching for wholesale and retail activities. MIFID II governs U.K. passporting, permitting a British licensed dealer to do business anywhere in the EU. The British had a lot of influence on the development of MIFID II, so the fear is that the Europeans will retract concessions, particularly in the areas of

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derivatives and futures trading. Like U.S. regulation, MIFID II requires research to be unbundled from services; Europeans, however, seem bent on returning research to its former status as a kickback.

Another case in point is fund management. London fund managers run $12 trillion, with a chunk coming from European investors. The EU directives for undertakings for collective investment in transferable securities, 2009/65/EC (for mutual funds), and alternative investment fund management (AIFM), 2011/61/EU (for hedge funds), had a lot of British input in their development. AIFM is currently under European Commission review in Europe, and managers complain about inconsistent application by member countries (FISMA/2016/105(02)/C).

The British convinced Europeans to permit funds managed outside the EU to be sold to EU-resident investors; most funds are domiciled in Luxembourg or the Caymans but not managed there. AIFM permits third-country managers to do business in the EU if their home countries have equivalent regulation, and it allows two types of EU passports: management and marketing. Before Brexit, the European Securities and Markets Authority (ESMA) was preparing to allow managers from 12 countries — including Switzerland and the United States — to have marketing passports to sell in the EU, but then put the kibosh on that project. The ESMA is now proposing new equivalence standards and reporting requirements. Without an EU passport, a fund would have to have a separate license in every country where it was marketed to investors. Funds still must register and may be restricted to institutional investors.

With Britain out of the EU, the seemingly uncontroversial management passport may yet be threatened. Fund managers fret that the EU will renew the 2017 effort to require that funds sold to the EU investors be managed in the EU, which at the time concluded that offerings would be discouraged and single market freedom would be impaired (COM (2017)147). No surprise that the French were behind that effort (*Financial Times*, Feb. 16, 2020). Back then ESMA complained about letterbox funds with no substance or managers on the ground (*Financial Times*, Jan. 3, 2018). Where have we heard that before?

ECOFIN put the Cayman Islands, a British overseas territory, on its blacklist of tax havens. This serves as a useful reminder that tax havens exist only as long as the developed countries with the customers tolerate them, like the brothel on the edge of town that the sheriff patronizes. Tax and banking havens do not exist in a state of nature; their money transfers have to be cleared.

The Caymans are a hedge fund haven that copies U.S. law to make American managers comfortable. The islands are part of a British empire of tax havens that feeds into London. Mostly the Caymans are used to funnel money from around the world into U.S. investment. Hedge funds sold to Europeans and directed as European investments tend to use Luxembourg, an EU member with a set of friendly laws. Like Guernsey, a crown dependency, the Caymans try to stay respectable for real businesses while keeping politically exposed persons and individual tax evaders out. But investment fund investor lists are secret.

The British empire of havens includes a lot worse, like the BVI, home to a lot of secret companies used by individuals to hide assets from their home governments. The Caymans were put on the EU gray list in 2017 for attracting investments with no real economic activity. Now the EU thinks the Caymans haven't done enough. The Caymans are being blacklisted for being uncooperative. Previously, British lobbying kept them off the blacklist.

The EU demands that the United Kingdom maintain standards on exchange of information and tax rulings. ECOFIN has approved some new recommendations for the code of conduct for income earned in blacklist countries or earned by blacklist residents. ECOFIN recommends that EU members deny deductions for payments to them, withhold on outbound payments, apply CFC rules, or deny benefits such as participation exemptions. Some EU members like France have their own blacklists with similar sanctions.

Brexit was a vote against continued immigration. The citizenship directive, 2004/38/EC, gives EU member country citizens the right to reside and work in another EU country. Since the Brexit vote, EU citizens have been staying away and some have returned to their home countries. Voters may not have understood that EU

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immigration is a small part of British immigration, most of which comes from former colonies. Be that as it may, the Johnson administration is taking steps to restrict unskilled immigration. Home Secretary Priti Patel announced that the United Kingdom would institute a points system to evaluate immigrants, which would require English fluency and a job offer. But visas for skilled immigrants will be fast-tracked and unrestricted in number (*The Wall Street Journal*, Feb. 19, 2020).

Regulatory Equivalence

How is an ex-royal grifter going to do business without a trademark? Queen Elizabeth II banned Prince Harry and Meghan Markle from using the trademark Sussex Royal for Instagram, products, or their charitable foundation, and also apparently banned them from using the word "royal" itself. Indeed, British company law doesn't let anyone call themselves royal, and royal souvenirs are only produced under temporary licenses. Look for the disgraced couple on the lecture circuit near you, reminding you of your obligations to the environment or the woke cause of the moment. Meanwhile, Prince Charles thinks the planet has only 10 years left (*Daily Mail*, Feb. 18, 2020).

Just as royal customs never change, neither do TheCityUK's arguments. Having accepted the inevitability of equivalent regulation, TheCityUK has put out yet another position paper arguing for structured cooperation, meaning both sides' regulators and industry consult with each other on regulatory changes and market access. Here the lobbyists are again assuming that the Europeans need London bankers rather than the other way around. It's like arguing that the royal family needs Meghan Markle.

TheCityUK is arguing for uninterrupted market access and autonomous regulatory decision-making based on regulatory outcomes. Thus the unilateral right of the Europeans to retract a determination of regulatory equivalence should be replaced with a process for maintaining equivalence and a requirement of withdrawal notice at least a year in advance. That process may include an arbitration mechanism for breaches. This argument is based on the binding commitments feature of the trade agreement that the EU has with Japan, which does not seem to be selling a lot of derivatives to Europeans (*Financial Times*, Feb. 12, 2020).

Likewise, Javid had been arguing for permanent equivalence, by which he apparently meant a long-term, managed framework of permissible divergence with assured market access. His approach was outed when his briefing paper was photographed by a paparazzo otherwise unoccupied with royals. The photograph showed a British demand for binding processes to stabilize equivalence. British regulators are working on equivalence agreements with the EU (*Financial Times*, Feb. 10, 2020).

Chief EU Brexit negotiator Michel Barnier says there will be no special treatment. He has also threatened to deny bank access to the European market if British fishing does not remain open to continental fishermen. The EU's revised negotiating position will insist on fishing rights. "The U.K. basically hates the unilateral nature of the equivalence decisions because it leaves a lot of the cards on the table for the EU. But that is just a fact of life," a Eurocrat told the *Financial Times* (*Financial Times*, Feb. 11, 2020).

Previously, we explained that the whole point of British fishermen regaining British fishing rights was to be able to sell more highly perishable langoustines to Europeans. Well, what do you know, French fishermen, acting on their puff, used their fishing boats to blockade Guernsey fishing boats' access to French ports to sell their catch. The French gripe was dilatory Guernsey issuance of interim licenses under the EU SMEFF regulation 2017/2403 to ensure French fishermen's access to British waters for the remainder of the year. Licenses were issued, the blockade was removed, and embarrassed Guernsey officials said the unofficial French action would not prejudice future negotiations. ■

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