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PART B

Part . B.

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PART B

Chancellor's (Lawson) Papers:

ECONOMIC FINANCE COUNCIL MEETINGS 1987

PO -CH /NL/0142
PART B

Disposal Directions: 25 Years

[signature]

25/8/95

The Commission would like the guidelines it has proposed and any conclusions of the Council to be taken into account in the national economic and budget policy debates and in the preparation of national public budgets for 1988.

The Council should examine this communication at its meeting on 13 July 1987.

It is also being submitted to the European Parliament and the Economic and Social Committee.

(Complimentary close).

(s.) Alois PFEIFFER

Encl.: COM(87) 297 final

ANNEX C2

EUROPEAN COMMUNITIES

THE COUNCIL

Brussels, 7 July 1987 (09.07)
(OR.f)

7625/87	
	RESTREINT

ECOFIN 39

miss Barber 20/G

mr. Savage IF2

TRANSLATION OF LETTER

from : Commission of the European Communities, signed by Mr Alois PFEIFFER, Member

dated: 3 July 1987

to : Mr Uffe ELLERMANN-JENSEN, President of the Council of the European Communities

Subject: Second quarterly examination of the economic situation in the Community

- Commission communication to the Council on the economic outlook for 1988 and budgetary policy in the Member States

C2

Sir,

I enclose a Commission communication on the economic outlook for 1988 and budgetary policy in the Member States.

In accordance with Article 3 of Council Decision 74/120/EEC on the attainment of a high degree of convergence of the economic policies of the Member States, this communication is being submitted with a view to the examination of the economic situation in the Community.

As provided for in the 1986/1987 Annual Economic Report, this communication includes an intermediate review of the application of the co-operative growth strategy for more employment.

.../...

In the margins

The Dutch might raise with you:

(g) Inter-American Development Bank - location of 1989 annual meeting;

Briefs on all these (except (c)) are attached, with single briefs covering (a) and (d) on the one hand and (b) and (e) on the other. Also attached is a table showing member states voting entitlements in the Council (Annex G).

"A" points

3. The list we have so far received is attached at Annex E.

4. We understand that the Dutch will want to make a unilateral statement for the minutes in relation to the Comitology Decision inviting the Commission to produce a revised text of the second Banking Co-ordination Directive with an article in it specifying the position and tasks of the Banking Advisory Committee. This is entirely acceptable to us. There will, however, be no discussion of the Danish statement. A short brief is at annex H.

Second quarterly review of the economic situation

5. A brief is at Annex A1. There will be a general exchange of views over lunch, and discussion will continue in the formal Council afterwards.

6. The July ECOFIN customarily conducts the second quarterly review of the economic situation, which is required by the 1987 Council decision on convergence of economic policies in the Community. Discussion is on the basis of a Commission paper (COM(87)297) attached at Annex A2. The paper will probably be introduced by Commissioner Pfeiffer.

7. The Council will be asked whether any changes should be made to the guidelines set out in the last annual economic report. The

45/13

FROM: J E MORTIMER
DATE: 9 JULY 1987

PAYMASTER GENERAL

ECOFIN 13 JULY

ECOFIN on 13 July, the first of the Danish Presidency, is in the Charlemagne in Brussels. You will be accompanied by Mr Lavelle, Mr Howard (C&E) and Mr Trevett (C&E). The meeting is scheduled to begin with lunch at 13.00, with the formal session beginning at 15.00.

2. The agenda is as follows:

Over lunch

(a) second quarterly review of the economic situation - general views;

(b) butter stock disposals (possibly);

(c) preparation for the informal ECOFIN in September.

In the formal Council

(d) continuation of discussion on second quarterly review;

(e) continuation of discussion on butter stock disposals;

(f) UK's request for a derogation under 6th VAT Directive (cash accounting).

Butter stock disposals

13. This is covered in Annex B1. The background papers are at Annexes B2-B5. Spain has asked for this item to be discussed over lunch. They also hope to make a short statement in the formal Council afterwards. It is not clear whether the Presidency has agreed to this procedure or whether they will insist on discussion being confined to the formal Council.

14. Delayed reimbursement for butter stock disposals was agreed by the Council in March. Nevertheless, the Spanish and Portuguese have protested at the financial burden it places on them, given that the stocks were built up before they joined the Community. Therefore ECOFIN asked the Commission to report on the points raised by the two new member states. The Commission produced its formal report just before the June ECOFIN, and at that meeting COREPER was asked to consider it and report back to this ECOFIN.

15. Most of the discussion is likely to be between the Spanish and Portuguese and the Commission. There should be no need for a UK intervention. We have no sympathy for Spain and Portugal on this point.

Preparation for the informal ECOFIN 12/13 September

16. There is no separate brief on this. We expect the Danish Presidency to outline a possible agenda, and perhaps say something about the administrative and social arrangements. No detailed discussion is expected.

17. The agenda will probably include:

- (a) preparation for the IMF/IBRD annual meetings;
- (b) strengthening of the EMS (arising mainly from French concerns following the January realignment);
- (c) liberalisation of capital movements. (The Monetary and Central Bank Governors Committees are studying the implications of full liberalisation prior to Commission proposals expected this autumn. At the European Council capital movements was picked out with some other internal

report was adopted last December, and the guidelines in it were reconfirmed by ECOFIN last March.

8. During discussion, you will want to argue against any changes in the guidelines. You could note - but not endorse - COM(87)297, while commenting on some of the points in it. You might also draw attention to the recent strength of the UK economy.

9. COM(87)297 argues that growth in the Community has slowed down, mainly due to a less favourable international environment. It argues that greater priority should be given to strengthening internal demand. On page 37, when discussing the UK, it says "...there could be a case for allowing the public sector borrowing requirement in 1988/89 to rise above the level set for the medium term". In our view, the general economic appraisal is a little gloomy, and the policy prescription for the UK unacceptable.

10. The Commission's paper was discussed at the Coordinating Group on 6 July, which Sir Peter Middleton attended, and its chairman will speak at the Council. A copy of Sir Peter's speaking notes for that meeting are attached at Annex A3.

11. The Commission paper and the economic outlook generally were discussed by the Economic Policy Committee on Wednesday. The chairman of this Committee, Mr Milleron, will also report to ECOFIN. A copy of the report he circulated to the EPC is at Annex A4. Mr Milleron is likely to say:

- the Commission's paper is a shade pessimistic. There may be rather more activity and a higher level of trade than was thought likely a month or two ago;
- it is important to retain flexibility in budgetary policy. We should see how things develop before taking further action.

We would not want to object to this.

12. The usual set of economic statistics is attached at Annex A5.

but there is no requirement to consult the European Parliament or the Economic and Social Committee.

22. We have been lobbying the French all week to withdraw their objection. The Chancellor spoke to Balladur over the telephone yesterday, but did not receive a helpful response (though whether because Balladur was not properly briefed or because he was not prepared to budge is not clear). Sir Geoffrey Littler will be talking to the French in Paris again today.

23. Your aim on Monday will be to exert maximum pressure on the French to withdraw their objection. If you fail, you will want to isolate France with a view to a Presidency conclusion making clear that they alone are blocking, quite unreasonably, the UK's derogation.

Inter-American Development Bank

24. This is covered in Annex D, supplied by ODA. It may be raised with you in the margins of the meeting by the Dutch.

25. The Inter-American Development Bank was set up in 1959 by the US to help development in Latin America. In 1976 European and some other countries joined, and once every four years the annual meeting is held on this side of the Atlantic. The next such occasion is in 1989. Four countries have been interested in hosting the meeting: Netherlands, Germany, Israel and Yugoslavia. The Dutch now claim to have squared the Germans, and may be seeking support against the other two countries. ODA suggest that we should support the Dutch.

Personality notes

26. These are attached at Annex F.

27. Copies of the briefing go to those on the list attached immediately beneath this covering minute.

JEM

J E MORTIMER

market areas for accelerated progress, ie complete liberalisation by end 1988);

(d) indirect tax approximation. This subject was going to be on the agenda for the July ECOFIN, but Lord Cockfield could not get Commission agreement on his detailed proposals in time for a July discussion.

Cash accounting and 6th VAT Directive - UK derogation

18. This is likely to be the most difficult item, but Mr Lavelle and Mr Howard have been closely involved in recent developments, and will be on hand to bring you up-to-date with what has been happening and advise on further action. The topic is covered in Annexes C1-C9.

19. Cash accounting for VAT for small and medium-sized enterprises was announced in the budget, and is intended to come into effect on 1 October. In the UK view, the relevant Community legislation (the sixth VAT directive) allows cash accounting on the "output" side (ie when the cash is received for supplies made) but does not in all circumstances allow cash accounting on the "input" side (when VAT is deducted on payment for supplies received). Therefore we need a derogation from the sixth VAT directive, as provided for in article 27 which allows member states to introduce simplified schemes.

20. In accordance with article 27 procedure, we notified the Commission in March about the new scheme, and they in turn notified other member states on 30 April. In the past, such requests from member states have been automatically approved by the Council after the specified notification period. However, in this case, the French have objected and have requested a Council discussion. The main French anxiety seems to be that they might come under pressure to introduce a comparable scheme.

21. Agreement to the derogation is necessary soon to meet the 1 October implementation date. On procedure, the Commission (which is content with our request) must now submit a proposal to the Council to provide for the UK derogation. Unanimity is needed for agreement,

CIRCULATION

Paymaster General
PS/Paymaster General
Sir Geoffrey Littler
Mr Lavelle
Mr Edwards
Mr C Budd, Cabinet Office
Mr J S Wall, FCO
Mr D Bostock, UKREP (8 copies)

Steering brief only

PS/Chancellor
PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Sir Peter Middleton
Mr Byatt
Mr P Cropper
Mr Scholar
Mr Culpin
Mr Matthews
Mr Kelly
Ms Sinclair
Mr Bonney
Mrs Imber
Mr Savage
The Governor B/E
Mr J Kirby B/E
Mr Garside - Paris
Mr A C Thorpe - Bonn
Mr T P Lankester - Washington
Miss C Elmes - Rome
Mr Wilmott C/E
Mr D Howard)
Mr P Trevett) C&E
Mr Crabtree ODA

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DICKINSON MAFF
PERRINS MAFF
THOMAS MAFF
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PS/PAYMASTER GENERAL TSY
LAVELLE TSY
EDWARDS TSY
MORTIMER TSY
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FRAME ECONOMIC/FRAME AGRICULTURE
ECOFIN COUNCIL : 13 JULY

SUMMARY

1. THE PAYMASTER GENERAL REPRESENTED THE UK.

'A' POINTS (SEE DOC 7670/87)

2. ALL AGREED EXCEPT ITEMS 13 (DELETED) AND 2A (WITHDRAWN AT SPANISH REQUEST DUE TO DRAFTING PROBLEMS AND TO BE RESUBMITTED TO COREPER).

SECOND QUARTERLY ECONOMIC REPORT.

3. AGREED. NO NEED TO CHANGE GUIDELINES IN 1986-7 ANNUAL REPORT. PREDICTABLE DIFFERENCE OF VIEWS ON COMMISSION CALL FOR COORDINATED FISCAL EXPANSION. SUBJECT LIKELY TO BE DISCUSSED AGAIN AT INFORMAL ECOFIN IN SEPTEMBER.

FINANCING OF BUTTER STOCKS DISPOSALS.

4. PORTUGAL ASKS FOR 24 MECU COMPENSATION: BELGIUM SHOWS SOME SYMPATHY, BUT NOT FOR LONG.

VAT CASH ACCOUNTING

5. UK DEROGATION AGREED FOR 3 YEARS, PENDING ADOPTION OF COMMUNITY RULES (22ND DIRECTIVE). COMMISSION TO REVIEW POSITION IF DIRECTIVE NOT IN PLACE BY THEN. MINUTES STATEMENT TO MAKE CLEAR DEROGATION IS WITHOUT PREJUDICE TO WORK ON THE DIRECTIVE. FINAL WORDING TO BE TIDIED BY COREPER FOR ADOPTION AS AN A POINT AT THE FOREIGN AFFAIRS COUNCIL ON 20 JULY. FRANCE APPARENTLY LOOKING FOR MOVEMENT ON DOM RUM.

LUNCH DISCUSSION

6. SEPTEMBER INFORMAL ECOFIN AND 1988 BUDGET AND REFERENCE FRAMEWORK.

7. FOR DETAILS SEE MY 4 IFTS.

HANNAY

ADVANCE
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LYALL-GRANT FCO
KERR FCO
WILLIAMSON CAB

/ ALTY

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FURTHER TAX CUTS BEYOND THE DM 14 BN PACKAGE (3/4 PERCENT OF GERMAN GDP) JUST PASSED BY PARLIAMENT AND THE PROPOSED INCREASE IN THE PUBLIC SECTOR DEFICIT WOULD BE COUNTER-PRODUCTIVE.

7. THE PAYMASTER GENERAL ALSO CONSIDERED THE COMMISSION'S PESSIMISM OVERDONE ESPECIALLY IN THE CONTEXT OF THE UK ECONOMY WHOSE PERFORMANCE IN THE LAST 12 MONTHS (PLUS 4 PERCENT INCREASE IN DEMAND) HAD OUTPACED EVEN THE MORE OPTIMISTIC FORECASTS: MOREOVER WITH LAST MONTH'S FALL IN UNEMPLOYMENT, THE LARGEST SINCE 1948, YET WITH REAL INCOMES RISING FASTER THAN PRODUCTIVITY THERE WAS CERTAINLY NO FURTHER STIMULUS NECESSARY.

8. ANDERSEN (DENMARK) ARGUED THAT WHILE THERE MIGHT BE NO NEED TO CHANGE THE GUIDELINES AGREED LAST YEAR IT WAS NECESSARY TO PURSUE THESE MORE EFFECTIVELY. THE LONGER THINGS WERE LEFT THE MORE DIFFICULT IT WOULD BE: DESPITE HER BALANCE OF PAYMENTS POSITION DENMARK WAS WILLING TO DO HER BIT BUT THERE WOULD HAVE TO BE A GUARANTEE THAT OTHER MEMBER COUNTRIES WOULD DO LIKEWISE.

9. PREDICTABLY MACSHARRY (IRELAND) SIMITIS (GREECE) AND CADILHE (PORTUGAL) SUPPORTED THE COMMISSION'S CALLS FOR AN INTENSIFICATION OF THE COOPERATIVE GROWTH STRATEGY AND FOR AN EMPHASIS ON BOOSTING DEVELOPMENTS IN THE ''LESS FAVOURED'' AREAS OF THE COMMUNITY. EYSKENS (BELGIUM) ALSO LENT SOME SUPPORT TO THE COMMISSION BY CALLING FOR A ''2 - TRACK POLICY'' I.E. TO CONTROL GOVERNMENT EXPENDITURE AND INFLATION AND REDRESS CURRENT ACCOUNT DEFICITS WHILE AT THE SAME TIME STIMULATING GROWTH BY NON-INFLATIONARY MEANS SUCH AS REDUCING FISCAL PRESSURE AND ENCOURAGING PRIVATE INVESTMENT. ON NORTH-SOUTH RELATIONS, HE SAID A COMMUNITY APPROACH TO ALLEVIATING INTERNATIONAL DEBT PROBLEMS WOULD CONTRIBUTE TO AN INCREASE IN WORLD TRADE WHICH WAS IN EVERYONE'S INTERESTS.

10. NIEMAN (NETHERLANDS) AND SCHEER (FRANCE) BOTH TOOK EXCEPTION TO SOME OF THE COMMISSION'S COMMENT ON BUDGETARY ASPECTS IN THEIR RESPECTIVE COUNTRIES, WHILE THE SPANISH ECONOMIC SECRETARY AND MORE VEHEMENTLY CADILHE DECLARED THE FORECAST'S FOR INFLATION IN THEIR COUNTRIES TO BE MUCH TOO HIGH. THE SPANISH MINISTER ALSO EXPRESSED CONCERN THAT ALTHOUGH DOMESTIC DEMAND IN SPAIN WAS HIGHER THAN THE COMMUNITY AVERAGE, THIS HAD LED NOT TO A REDUCTION IN UNEMPLOYMENT AT HOME BUT AN INCREASE IN THE TRADE DEFICIT: SO THERE WAS A CLEAR NEED FOR GREATER ACTION BY THE STRONGER ECONOMIES.

11. SIMOUSEN (PRESIDENCY) CONCLUDED THAT THERE WAS NO NEED TO CHANGE THE ECONOMIC POLICY GUIDELINES SET OUT IN THE LAST ANNUAL ECONOMIC REPORT. THE ECONOMIC SITUATION IN THE COMMUNITY SHOULD BE CAREFULLY MONITORED AND RECONSIDERED AT THE SEPTEMBER INFORMAL /ECOFIN

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FRAME ECONOMIC
ECOFIN COUNCIL : 13 JULY
SECOND QUARTERLY ECONOMIC REVIEW

SUMMARY

1. AGREED NO NEED TO CHANGE GUIDELINES IN 1986-7 ANNUAL REPORT. PREDICTABLE DIFFERENCE OF VIEWS ON COMMISSION CALL FOR COORDINATED FISCAL EXPANSION. SUBJECT LIKELY TO BE DISCUSSED AGAIN AT INFORMAL ECOFIN IN SEPTEMBER.

DETAIL

2. THE COUNCIL DISCUSSED THE COMMISSION'S JULY COMMUNICATION ON THE ECONOMIC OUTLOOK (7625/87), WHICH RECOMMENDED NO CHANGE IN THE GUIDELINES FOR BUDGETARY POLICY IN THE LAST ANNUAL ECONOMIC REPORT BUT URGED THAT THEY BE MORE SPEEDILY IMPLEMENTED: CALLED FOR A JOINT PROGRAMME OF FISCAL EXPANSION IN 5 MEMBER STATES WITH A RELATIVELY FAVOURABLE PUBLIC FINANCE SITUATION (DENMARK, GERMANY, FRANCE, LUXEMBOURG AND THE UNITED KINGDOM): AND (A PROCEDURAL INNOVATION) ASKED FOR ITS COMMUNICATION AND THE RESULTS OF THE COUNCIL'S DISCUSSION TO BE BROUGHT TO THE ATTENTION OF NATIONAL PARLIAMENTS.

3. CHRISTOPHERSEN (COMMISSION), DEPUTISING FOR PFEIFFER, INTRODUCED THE COMMISSION'S COMMUNICATION.

4. THE CHAIRMAN OF THE COORDINATING COMMITTEE AND ECONOMIC POLICY COMMITTEE REPORTED ON THEIR COMMITTEES' DISCUSSION OF THE COMMISSION'S COMMUNICATION. THERE WAS GENERAL AGREEMENT THAT THE POLICY GUIDELINES SET LAST DECEMBER SHOULD NOT BE CHANGED BUT A DIVISION OF VIEWS ABOUT THE COMMISSION'S CALLED FOR FISCAL EXPANSION, SOME DELEGATIONS SUPPORTING THE COMMISSION, OTHERS UNDELINING THE IMPORTANCE OF A FIRM MEDIUM TERM APPROACH AND THE RISKS OF EXPANSIONARY POLICIES. THE COORDINATING COMMITTEE ENDORSED THE COMMISSION'S DECISION TO SEND ITS COMMUNICATION TO THE EUROPEAN PARLIAMENT AND ECONOMIC AND SOCIAL COMMITTEE BUT CONSIDERED THAT IT WAS FOR INDIVIDUAL GOVERNMENTS TO DECIDE HOW OR WHETHER IT SHOULD BE PRESENTED TO NATIONAL PARLIAMENTS.

5. THERE FOLLOWED A LENGTHY TABLE ROUND IN WHICH MOST MINISTERS READ OUT PREPARED STATEMENT, MANY REPEATING POINTS ALREADY MADE OVER LUNCH.

6. SCHIECHT (GERMANY) THOUGHT THE REPORT TOO PESSIMISTIC ESPECIALLY AS REGARDS GERMAN ECONOMIC PERFORMANCE. BUT IN ANY CASE HIS GOVERNMENT WAS DOING AS MUCH AS POSSIBLE TO BOOST DEMAND: ANY

/FURTHER

ECOFIN. MEMBER STATES SHOULD DECIDE INDIVIDUALLY HOW FAR NATIONAL PARLIAMENTS SHOULD BE INFORMED OF THE COMMISSION'S AND COUNCIL'S VIEWS.

HANNAY

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PS/CHANCELLOR TSY
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PMP

2788/25

FROM: J E MORTIMER
DATE: 14 JULY 1987

1. Mr Lavelle 14/7

2. Paymaster General

cc: PS/Chancellor
Sir G Littler
Mr Edwards
Mr Scholar
Mr Matthews
Mr Bonney
Miss Barber
Mr Dyer
Mr Howard (C&E)

ECOFIN, 13 JULY

I attach for approval a draft arranged Parliamentary Question and Answer reporting on Monday's ECOFIN.

2. Perhaps your office could let Parliamentary Section know if you are content with it.

J E MORTIMER

ECOFIN ARRANGED PQ

..............................To ask the Chancellor of the Exchequer if he will make a statement on the outcome of the Economic and Finance Council meeting on 13 July.

DRAFT REPLY BY THE PAYMASTER GENERAL

This meeting was held in Brussels. I represented the UK.

The Council carried out its second quarterly review of the economic situation in the Community. It was agreed that there was no need to change the economic policy guidelines contained in the annual economic report adopted last December.

Spain and Portugal reiterated their concern about the impact on them of the Council's decision to delay reimbursement to member states of losses incurred on the disposal of butter stocks. The Council took note of their views.

The Council agreed to a UK request for a derogation from the sixth VAT directive relating to cash accounting for small businesses. The derogation will apply for a transitional period until the Council adopts a Community wide scheme. The Council will review the position after three years.

PAYMASTER GENERAL

FROM: APS/Paymaster General
DATE: 14 July 1987

RP

APS/CX

MR HOWARD - C&E

cc PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Mr Lavelle
Mr Scholar
Miss Sinclair
Mr Cropper
Mr Trevett - C&E
PS/C&E
Mr Bostock - UKREP

CASH ACCOUNTING: EC DEROGATION

The Paymaster General discussed the derogation with the Chancellor last night. Although the EC Council Secretariat will be preparing a draft text of the derogation, the Paymaster General would be grateful if you could urgently draw up our draft text which could be presented to the Danish Presidency.

2. In particular, it would be useful if a form of words could be found which suggest that the derogation is more permanent and for three years only in the first instance, so that renewal can be made as automatic as possible.

Deborah Francis.

MISS D L FRANCIS
Assistant Private Secretary

FROM: P TREVETT
DATE: 14 JULY 1987
HM CUSTOMS AND EXCISE
VAT CONTROL DIVISION D
ALEXANDER HOUSE 21 VICTORIA AVENUE
SOUTHEND-ON-SEA X SS99 1AJ
TELEPHONE SOUTHEND-ON-SEA (0702) 348944 ext

Paymaster General

cc PS Chancellor
PS Chief Secretary
PS Financial Secretary
PS Economic Secretary
Mr Lavelle
Mr Scholar
Miss Sinclair
Mr Cropper
Mr Bostock (UKREP)

CASH ACCOUNTING DEROGATION : ECOFIN DECISION

Your Private Secretary's minute to Mr Howard of today's date.

2. We have provided UKREP with the attached text, which they have fed in to the Council:-

"This Decision shall apply from 20 July 1987 for a transitional period until the Council, acting unanimously on a proposal from the Commission, adopts a community special scheme for small and medium sized businesses. If, however, at the end of 3 years such a scheme has not been adopted, the Commission shall examine the United Kingdom's system of cash accounting and report on its operation to the Council".

3. We hope to know tomorrow whether this suggested text has been accepted by the Presidency and, if not, what alternative text they have proposed for agreement in COREPER. We shall report back to you as necessary.

PT

P TREVETT

Internal Distribution

CPS
Mr Knox
Mr Howard
Mr Jefferson Smith
Mr Wilmott
Mr Cockerell
Mr Holloway

EC1/005/njo

FROM: J E MORTIMER

DATE: 15 July 1987

CHANCELLOR OF THE EXCHEQUER

cc Paymaster General
Sir Geoffrey Littler
Mr Lavelle
Mr Edwards
Mr Scholar

CABINET, 14 JULY: OUTCOME OF JULY ECOFIN

You might care to report to Cabinet tomorrow the outcome of the July ECOFIN:

- The Paymaster General represented the UK. The Council carried out its second quarterly review of the economic situation. It was agreed that there was no need to change the economic policy guidelines contained in the Annual Economic Report adopted last December.

- Spain and Portugal reiterated their concern about the impact on them of the Council's decision to delay reimbursement to member states of losses incurred on the disposal of butter stocks. The Council took note of their views.

- the Council agreed to a UK request for a derogation from the sixth VAT directive relating to cash accounting for small businesses. The derogation will apply for a transitional period until the Council adopts a Community wide scheme. The Council will review the position after three years.

2. You will be aware that we have been concerned about what would happen to our VAT cash accounting derogation at the end of the three year period agreed in ECOFIN. We had hoped that the derogation would continue until the Council took a positive decision to end it. We were not able to achieve

this, however. To secure the derogation now, it has been necessary to accept that we may have to apply for an extension to the derogation in three years' time. The exact form of words governing what will happen has yet to be agreed in COREPER. There is, however, probably no need for you to go into this detail with your Cabinet collegues.

see below

J E MORTIMER

396/32

FROM: S P JUDGE
DATE: 15 July 1987

PAYMASTER GENERAL

MR TREVETT (*)

cc
PS/Chancellor
PS/Chief Secretary
PS/Financial Secretary
PS/Economic Secretary
Mr Lavelle
Mr Scholar
Miss Sinclair
Mr Cropper
Mr Bostock (UKREP) (*)
(* advance copy
by fax)
PS/C&E

CASH ACCOUNTING DEROGATION: ECOFIN DECISION

The Paymaster General has seen your submission of today, and is content with Customs' view - which he assumes is shared by UKREP.

2. He thinks there is a good case for the amendments you propose, on the basis of Monday's debate at ECOFIN.

3. If the amendment is not accepted, then he would like to see an entry in the minutes to the effect that we wish to see the derogation maintained, in the context of orderly support for SMEs in the UK. You told me that UKREP were thinking on similar lines.

SPJ

S P JUDGE
Private Secretary

396/40

RP

FROM: APS/Paymaster General
DATE: 20 July 1987

MR J E MORTIMER

cc PS/Chancellor
Sir G Littler
Mr Lavelle
Mr Edwards
Mr Scholar
Mr Matthews
Mr Bonney
Miss Barber
Mr Dyer
Mr Howard (C&E)

ECOFIN, 13 JULY

The Paymaster General was grateful for your minute of 14 July attaching a draft arranged Parliamentary Question and Answer.

2. The Paymaster has now approved the draft Answer and I would be grateful if the Parliamentary Clerk could arrange for the Answer to be laid today.

Deborah Francis.

MISS D L FRANCIS
Assistant Private Secretary

3874/18

G32

CONFIDENTIAL

cc PS/CHANCELLOR
PS/CST
SIR P MIDDLETON
MR FER BUTLER
SIR G LITTLER
MR LAVELLE, MR EDWARDS.

FROM: PAYMASTER GENERAL
DATE: 27 July 1987

MR BONNEY, MR CRABBIE,
MR MORTIMER, MR DONNELLY,
MR CROPPER,
MISS WHELDON - T/SOL.

PRIME MINISTER

BUDGET COUNCIL: 23 JULY

The Budget Council failed last week to agree a draft Community budget for 1988, and decided to meet again on 17 September.

2. The Danish Presidency argued hard for a draft budget which would have exceeded the 1.4 per cent VAT ceiling by 5.66 billion ecu (equivalent to a VAT rate of about 1.7 per cent). At the request of the Germans and ourselves, however, the Council Legal Service confirmed that the Council could not legally put forward a draft budget which exceeded the own resources ceiling unless there was unanimous agreement by member states that the extra resources would be provided. I made clear that there was no question of the UK agreeing to this. The Germans, too, argued that the draft budget must respect the 1.4 per cent ceiling, and the Spanish argued that it would be wrong to prejudge the outcome of the future financing negotiations.

3. The Council Legal Service also said that the European Court's case-law (not the Treaty) pointed to a principle of 'continuity of the Community' and 'veracity' in the establishment of the budget. On this flimsy basis, the other southern member states and Ireland persisted in arguing for raising the Presidency's expenditure proposals, while the other northern member states, including France, argued for going beyond 1.4 per cent - though not as far as the Presidency or the Commission had proposed.

4. By early evening it became clear that no agreement was possible. At no stage was the UK abatement mentioned: the gulf which separated the large and small spenders was too great to be bridged by any plausible adjustment to it.

1/2 8/-

5. It is not clear what the Presidency will do when the Council resumes in September. It would be difficult for the Council to brush aside the Council Legal Service's advice and establish a draft budget in excess of the 1.4 per cent VAT ceiling. Even if they were minded to do so, I would hope that no qualified majority would be found for such a budget. The Germans have told us that they will not be willing to compromise on the 1.4 per cent issue this side of the Copenhagen European Council, and the Dutch too have told us that, much as they would prefer a larger budget, their present view is that they cannot vote for a budget in which expenditure exceeds the 1.4 per cent ceiling unless there has been unanimous agreement by all member states to provide the extra resources.

6. On the other side of the argument, the southern member states and Ireland, and likewise Belgium, Luxembourg, Denmark and France, will not readily agree to respect the 1.4 per cent ceiling when the resulting budget proposals would in their view be manifestly inadequate in relation to the Community's needs, as well as being unacceptable to the Parliament. The Presidency might try to commend to the Council some ruse such as placing revenue beyond the 1.4 per cent ceiling in square brackets. This would not, however, remove the legal constraint that expenditure in the budget cannot without unanimous prior agreement exceed the revenues available within the 1.4 per cent ceiling.

7. The Presidency's best strategy, I suspect, will be to try to establish a draft budget within the 1.4 per cent ceiling with an accompanying Council declaration that the Commission and Council will act with all possible speed to amend the budget after the Copenhagen European Council if that Council reaches a firm decision to increase the Community's revenues. I believe we should be prepared to accept a non-prejudicial declaration along these lines, though the precise language would need to be carefully watched. The President of the Budget Council may wish to discuss this when he visits me in the first week of September.

8. It is by no means impossible that the Council will again fail to reach agreement in September and will then miss the 5 October deadline in the Treaty for submitting a draft budget to the Parliament. The budget procedure might well then remain stalled until after the Copenhagen European Council. It is also highly likely, however, that the European Parliament would reject any draft budget which the Council did agree to put forward, so the budget procedure may well be stalled in any case until after Copenhagen. This would not, I think, be a disaster from the UK's point of view.

9. Whatever the outcome may be, I suggest the priorities for the UK should continue to be to beat off any challenge to our abatement, and to avoid prejudging or prejudicing the outcome of the future financing negotiations.

10. I am copying this minute to Geoffrey Howe, John MacGregor and the Attorney General: and to Sir Robert Armstrong.

P.B.

PETER BROOKE

JMG 28 JUL 1987 — 13

CONFIDENTIAL

G32

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

28 July 1987

Dear Simon,

BUDGET COUNCIL: 23 JULY

The Prime Minister has considered the Paymaster General's minute of 27 July about the recent EC Budget Council. She has commented that she does not share the view that the suggested Council declaration, mentioned in paragraph 7 of Mr. Brooke's minute, is non-prejudicial. In her view it leads to clear expectations that the Budget will be increased. We shall need to consider this point further.

I am copying this letter to the Private Secretaries to the Foreign and Commonwealth Secretary, the Minister of Agriculture, the Attorney General and Sir Robert Armstrong.

Yours sincerely,

Charles Powell

Charles Powell

Mr Bonney
Mr Crabtree
Mr Mortimer
Mr Donnelly
Mr Cropper
Miss Wheldon - T/Sol
Mr Bostock UKREP

PAYMASTER GENERAL'S OFFICE	
REC.	28 JUL 1987
ACTION	Mr Edwards
	PS/Chlex
	PS/CST
	Sir P Middleton
	Sir G Littler

Mr FER Butler
Mr Lavelle

Simon Judge, Esq.,
Paymaster General's Office,
H.M. Treasury.

CONFIDENTIAL

BIF 24/8

Pse remind me when
Sir G is back

Sir G returns to office
~~24~~/8.

BIF 25/8.

Sir G Littler
Mr Allan
Miss Barber
PS/Governor - BOE

BF ~~12/8~~ 17/8

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

31 July 1987

P Simonsen Esq
Minister of Finance
12 Slotsholmsgade
DK-1216 Copenhagen K

BF to Jonathan
~~6/8~~

Has Geoff fixed time with Tradet?

Dear Mr Simonsen

INFORMAL ECOFIN MEETING: SEPTEMBER 1987

The Chancellor of the Exchequer has asked me to thank you for your letter of 22 July setting out further details about the Informal ECOFIN meeting to be held from 11-13 September 1987 in Denmark.

... Please find enclosed the completed questionnaire. I would like to point out that all five members of the UK Delegation will be travelling to Denmark together, on the flight indicated in the questionnaire, and will require transport from Beldringe airport to the hotel Hesselet, on Friday 11 September.

However, on the return journey, the Chancellor and Sir Geoffrey and Lady Littler will be travelling separately from the Governor and Mrs Leigh Pemberton. The Chancellor, Sir Geoffrey and Lady Littler will be returning on a private plane, an HS125, departing Beldringe airport, on Sunday 13 September at 14.45. They will therefore require transport from Faaborg to Beldringe airport after lunch on Sunday. The Governor and Mrs Leigh-Pemberton will be flying from Odense airport to Copenhagen on flight DX310, departing Odense at 16.25, on Sunday 13 September. They will therefore require transport from Faaborg to Odense airport after lunch on Sunday.

Please could you also note that I will be on leave from 19 August and therefore, the person to contact from this day onwards will be Mrs Cathy Ryding on 01-270-5004.

Yours sincerely

Julie Long

MISS J LONG
Diary Secretary

QUESTIONNAIRE:

Contact person in the Ministy:

Name: Miss J Long until 18/8/87 from 19/8/87 Mrs Cathy Ryding

Telephone no.: 01-270-5011 01-270-5004

Informal ECOFIN-meeting September 11,12,13 1987

The names of participants in the delegation:

Minister of Finance/Economic Affairs	Rt Hon Nigel Lawson MP
Spouse:	--- ....
Governor of Central Bank	Robin Leigh-Pemberto
Spouse:	Rose Leigh-Pemberto
Government official	Sir Geoffrey Littler
Spouse:	Lady Shirley Littler

Transportation:

Arrival:

A. Airline: Flight number	..........---....
Arrival at Kastrup Airport, Copenhagen	..........---....
B. Private plane: Type and immatriculation	HS125
Date and time of arrival	11/9/87 17.00
Parked at Beldringe airport in the weekend	YES
C. Car type and immatriculation	..........---....
Date and time of arrival at the Danish border	..........---....

Departure.

A. Airline: Flight number DX310
Departure from ODENSE Airport 13/9/87 16.25

B. Private plane: Type and immatriculation HS125
Date and time of departure 13/9/87 14.45

C. Car. Date and time of departure ......---......

Persons accompanying:

Driver's name: ......---......
Name(s) of security personneal ......---......
Registration number of weapons, if any ......---......

Other information:

	Delegation member.	Spouse.
Blood type		
Ministers	---	---
Governor of Central Bank	---	---
Government official.	---	---

Does any person in the delegation need special diet?

NO

Please do not hesitate to contact Mr. Hilmar Bojesen if you have any more questions (1924158.)

CONFIDENTIAL

7a

CC PS/CHANCELLOR
PS/CST
SIR P. MIDDLETON
SIR G. LITTLER
MR FER BUTLER
MR LAVELLE, MR BONNE
MR EDWARDS, MR CRABBIE,
MR MORTIMER,
MR DONNELLY
MR GROPPER
MR BOSTOCK UKREP

Treasury Chambers, Parliament Street, SWIP 3AG

31 July 1987

Charles Powell Esq
Private Secretary to the Prime Minister
10 Downing Street
London SW1

Dear Charles

COMMUNITY BUDGET FOR 1988

Thank you for your letter of 28 July.

The Paymaster General quite takes the Prime Minister's point that a Council Declaration on the lines envisaged in paragraph 7 of his minute of 27 July would create a clear expectation that the budget would be increased if the Copenhagen European Council agreed to provide the Community with extra revenues. In his view the Council would decide to raise the budget in that event; we also have to bear in mind that a budget which is limited to 1.4 per cent VAT, while making full provision for the UK's large abatement entitlement, will undershoot the agreed 1988 budget discipline limits by some 1380 mecu.

The Paymaster General wished to make a rather different, though related, point - namely that a Council Declaration of willingness to raise the budget if more revenues were provided would not prejudice the critical question of whether more revenues should be provided. Subject to the Prime Minister's views, the Paymaster General thinks that it would be difficult for the UK to oppose a suitably worded Declaration in this sense, if the Presidency and other Member States wanted it, and in the context of a draft budget which met our requirements in full by respecting the 1.4 per cent ceiling and making full provision for the UK's abatement.

The Paymaster General suggests that we wait and see what the Danish President of the Budget Council has to say when he comes to London in the first week of September, and take stock again thereafter, before the meeting between the Prime Minister and Christophersen (which the Paymaster believes could be extremely helpful in the future financing context), and before the Budget Council resumes on 17 September.

I am copying this letter to the Private Secretaries to the Foreign and Commonwealth Secretary, the Minister for Agriculture, the Attorney General and Sir Robert Armstrong.

Yours ever

Simon Judge

S P JUDGE
Private Secretary

ECON SIT IN GREECE
E

INFORMAL ECOFIN 11-13 SEPTEMBER 1987 **ANNEX E**

ECONOMIC SITUATION IN GREECE

Attached are:

(1) background brief by IF

(2) Council Decision on Greece's Community Loan

ECONOMIC SITUATION IN GREECE

1. Expansionary policies in the early 1980s contributed to mounting balance of payments and budget deficits and high rates of inflation.

2. Following the general elections of June 1985, the Government announced a redirection of policies, with the immediate emphasis on reducing the balance of payments deficit.

3. The important Stabilisation Programme introduced in October 1985 included: (a) a reduction in the PSBR of about 4 per cent of GDP in both 1986 and 1987, to be achieved by tax increases and spending cuts; (b) a tightening of monetary policy through lower DCE limits and increases in interest rates; (c) a 15 per cent devaluation of the drachma; (d) a modification of the compulsory wage-indexation scheme (to exclude the impact of import prices and to index wages to expected rather than past price increases) which implied substantial cuts in real earnings.

4. In the event, real personal disposable incomes were reduced by almost 5 per cent in 1986. A 20 per cent cut in public investment also depressed domestic demand. Yet real GDP rose moderately, because of rising exports and strong growth of agricultural output. This year real GDP is likely to fall however, given a continuing decline in consumers' real income and their expenditure and a big drop in farm output because of bad weather.

E1

5. The current balance of payments deficit halved, to 4¼ per cent of GDP, in 1986, partly because of the increase in exports, but chiefly because of the fall in oil prices and a significant increase in net EC transfers (which together account for four-fifths of the improvement).

6. The PSBR fell by about 4 per cent as intended, from 17.6 per cent of GNP in 1985 to 13.7 per cent of GDP. The introduction of VAT this January and low public pay increases are expected to reduce the PSBR further this year (to about 12½ per cent of GDP), but not by as much as was originally planned.

7. The inflation rate peaked at 25 per cent at the end of 1985, declined to 17 per cent by the end of 1986, but then temporarily picked up again early this year after the introduction of VAT. In June, consumer prices were 18 per cent higher than a year before.

8. The following table gives some summary statistics for 1985 and 1986 and OECD forecasts for 1987.

	1985	1986	1987
Real GDP*	2.1	1.3	-1
Manufacturing production*	4.5	0.5	3/4
Unemployment rate (%)	8.6	8.1	8 3/4
Consumer prices*	18.5	22.3	14 3/4
Current balance ($bn)	-3.3	-1.7	-1½

* Percentage changes.

TARGETS AND PERFORMANCE

On 9 December 1985 the Council, consequent to approving a loan to support Greece's balance of payments, stipulated targets for 1986 and 1987 against which to measure the progress of the Stabilisation Programme. (These are additional to the Greek authorities' own targets.) The targets are compared below with performance so far.

		Target	Performance
i.	Inflation		
	1986	15% at end-year (Greek stabilisation programme set 16%).	15.9% at end-year.
	1987	10% mid-year, excluding effects of VAT introduced on 1 January (Greeks' target for end year, including VAT, now revised up from 10% to 13.2%).	18.1 % in June (including VAT).
ii.	Wage Policy		
	1986 and 1987	Appreciable slowdown in increase of labour costs through adjustment of wage indexation mechanism (based on future inflation rate and excluding import prices).	Real average earnings estimated to have declined by 8½% between 1985 & 1986. Nominal increases of 8-9% expected in 1987 (i.e. below inflation rate).
iii.	PSBR		
	1986	Reduction in PSBR:GDP ratio of 4%.	Net PSBR (cash basis) reduced from 17.9% of GDP in 1985 to 13.7% in 1986.

	1987	Further reduction in PSBR:GDP ratio of 4%.	Officially forecast in June to be 11.3% of GDP this year.
iv.	Monetary Policy		
	1986	Reduction in DCE to 17% by end-year and reduction in proportion of PSBR covered by monetary resources.	DCE reduced to 18.2%. Little success in increasing recourse to non-bank private sector in financing PSBR.
	1987	Reduction in DCE to 11% by end-year (13.2% was originally cited as target in Monetary Programme; now set at 11.2%).	15% in April. Overrun for year as a whole seems likely.
v.	Balance of Payments		
	1986	Reduction in current account deficit necessary to stabilise external public debt by 1988. Greeks' target $1.7 bn.	Current account deficit reduced to $1.7 bn in 1986 from $3.3 bn in 1985.
	1987	Greek authorities' target $1.25 bn for current account deficit.	Cumulative deficit for January-May of $1.44 bn in 1986). Greeks now forecast $1.35 bn for 1987.

To summarise, while the current account and PSBR targets were met last year, this largely reflected favourable external developments and the outturns might even be regarded as disappointing under such circumstances. The evidence so far available for this year suggests that (although there may be a further fall in real wages) it will be virtually impossible to meet the targets for inflation and the balance of payments, and there are also likely to be difficulties with the fiscal and monetary targets.

COUNCIL DECISION

of 9 DEC. 1985

concerning a Community loan in favour
of the Hellenic Republic

THE COUNCIL OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic Community,

Having regard to Council Regulation (EEC) No 682/81 of 16 March 1981 adjusting the Community loan mechanism designed to support the balance of payments of Member States ([1]), as amended by Regulation (EEC) No 1131/85 ([2]), and in particular Article 2 thereof,

Having regard to the proposal from the Commission, submitted after consultation of the Monetary Committee,

E2

([1]) OJ No L 73, 19.3.1981, p. 1.
([2]) OJ No L 118, 1.5.1985, p. 59.

.../...

Whereas examination by the Commission, in collaboration with the Monetary Committee, of the economic situation of Greece has shown a marked deterioration in the balance of payments, a fall in the foreign exchange reserves and a rapid increase in external indebtedness; whereas these difficulties, because of their persistence are liable to jeopardize the proper functioning of the common market;

Whereas the Greek Government has applied for a medium-term loan under the Community loan mechanism designed to support the balance of payments of Member States; whereas the granting of such a loan is an appropriate measure, within the framework of mutual assistance, to facilitate the adjustment of the Greek economy;

Whereas the main reasons for the deterioration in the balance of payment of Greece are the absence of control over domestic factors, notably a sharp acceleration of inflation, a rapid rise in labour costs, a marked deterioration in the situation of the productive sector and a substantial over-run of domestic budgetary and monetary targets;

Whereas the Greek authorities have adopted an economic recovery programme and have presented this programme at the same time as their application for a loan; whereas the Commission has addressed to the Greek Government a recommendation on the measures which it suggests should be adopted; whereas the Greek authorities have approved the terms of the said recommendation;

Whereas the Greek Government, in implementing this recovery programme, undertakes to pursue, over a period of two years, and if necessary taking the appropriate corrective measures during the period, the following objectives:

1) a slowdown of inflation, so that the annual rate of price increase is brought down to 15% at the end of 1986 and to under 10% by mid-1987, excluding the effects of the introduction of value added tax from 1 January 1987;

2) a very appreciable slowdown in the upward movement of labour costs, through a lasting adjustment of the wage indexation mechanism based on an advance inflation norm and excluding from wage adjustments rises in import prices;

3) a reduction in the public sector borrowing requirement of 4 percentage points of the Gross Domestic Product in 1986 and of a similar amount in 1987;

4) a progressive but substantial reduction in domestic credit expansion to 17% in 1986 and to 11% in 1987 compared with 25% in 1985 and a significant reduction in the proportion of the public sector borrowing requirement covered by monetary resources;

5) a reduction in the current account deficit so that as early as 1988 the external public debt can be stabilized in terms of absolute value;

.../...

Whereas the implementation of this programme is to give priority, within a medium-term perspective, to strengthening and modernizing productive structures; whereas as a result the conditions for the recovery of productive investment are to be established;

HAS ADOPTED THIS DECISION:

Article 1

The Community shall grant the Hellenic Republic, under Regulation (EEC) No 632/81, a loan of 1 750 million ECU or the equivalent amount in other currencies.

Article 2

The loan shall be made available to the Hellenic Republic in two equal instalments:

- the first instalment as soon as the borrowing operations are completed,

- the second instalment within one year of the payment of the first instalment, and, in any case, not before 1 January 1987, the Commission shall release the second instalment in the light of the examination, made in collaboration with the Monetary Committee, of the evolution of the economic situation of the beneficiary Member State and the results obtained in the execution of the economic recovery programme, as implemented.

.../...

Article 3

1. The loan shall be granted on the basis of the decision taken by the beneficiary Member State to implement the economic recovery programme which it has presented, the objectives of which are set out in the recitals to this Decision.

2. The Commission, in collaboration with the Monetary Committee, shall examine at regular intervals the evolution of the economic situation of the beneficiary Member State and the execution of the econòmic recovery programme, as implemented.

Article 4

This Decision is addressed to the Hellenic Republic.

Done at Brussels, 9 DEC. 1985

For the Council
The President

(s.) J.SANTER

Certified true copy
For the Secretary-General

Wolfgang PINI
Director-General

CAPITAL CONVERGENCE
F

ECOFIN 11-13 SEPTEMBER 1987

Aide Memoire on Capital Convergence (for possible discussion with Stoltenberg)

- You attach great importance to the success of the current discussions aimed at securing convergence of capital adequacy requirements in both the EC and G10 countries. To include the USA and Japan in an agreement would be a major prize, which is well within our grasp if enough political weight is put behind it.

- Germany's support is especially important. You hope Stoltenberg will do everything he can at his end to see that this major opportunity is not missed.

- You understand there have been particular problems over the definition of capital, but that the Bank believe they have identified a basis for compromise (which gives due prominence to a very narrow definition of top quality capital). You are sure any remaining problems can be sorted out, given enough will; and you hope German officials will get in touch with the Bank if there are any difficulties to try to sort them out on a bilateral basis.

- Time is short. The next few weeks, but especially the Basle supervisors committee meeting on 16-18 September and EC Council working group discussions on the "Own Funds Directive" will be vital if the USA and Japan are to be included in an agreement by the end of the year.

F

BF 25/8

1. X & Y are [illegible], & obviously linked. Makes sense, given McPherson's background.

obviously

linked

2. What is state of play on Lawson/Baker talks on these & other matters, post [illegible]?

GRS 650

Restricted

RESTRICTED
FROM UKDEL IMF/IBRD WASHINGTON
TO DESKBY 050900Z FCO
TELNO 202
OF 042130Z AUGUST 87

SUB SAHARAN AFRICAN DEBT: WORLD BANK FOLLOW UP

SUMMARY

WORLD BANK CONSIDERING FOLLOW-UP TO JULY 10 MEETING, PARTICULARLY INTEREST RATE REDUCTIONS AND COFINANCING PROSPECTS. MISSION PLANNED TO DONOR CAPITALS IN THE COURSE OF SEPTEMBER. SUBSEQUENT GENERAL MEETING UNDER CONSIDERATION, PERHAPS LATE OCTOBER.

DETAIL

2. JAYCOX (VP AFRICA) CAME TO SEE ME AND LEADER TO DISCUSS FOLLOW UP TO THE PARIS MEETING ON SUB SAHARAN AFRICAN DEBT. JAYCOX EXPRESSED APPRECIATION OF THE UK CONTRIBUTION AT THE PARIS MEETING. HE ASSESSED PROSPECTS FOR THE THREE MAIN PROPOSALS ON THE TABLE AS FOLLOWS:

I. SAF TREBLING: AS SEEN BY THE BANK, A GOOD MANY PROBLEMS REMAIN, AND THE BANK WERE CONCERNED THAT THE PROPOSAL WAS SEEN AS COMPETITIVE WITH THEIR OWN COFINANCING IDEA: UNLESS THERE IS ADDITIONALITY, SAF TREBLING WOULD NOT HELP THE AFRICAN COUNTRIES,

II. ON THE PROPOSAL FOR ENHANCED COFINANCING WITH THE BANK FOR STRUCTURAL ADJUSTMENT, THIS SEEMED TO HAVE RECEIVED GENERAL SUPPORT, AND THE BANK PROPOSED TO PURSUE IT AS BELOW,

III. ON INTEREST RATE CONCESSIONS IN THE PARIS CLUB, THE PARIS MEETING WAS SOMEWHAT DISAPPOINTING BUT THE BANK HAVE NOT GIVEN UP HOPE. A GOOD DEAL OF WORK SEEMED TO BE GOING ON WITHIN THE US ADMINISTRATION, THOUGH LITTLE WAS BEING SAID ABOUT IT. FRANCE WAS QUOTE WAVERING UNQUOTE, IN SPITE OF TRICHET'S NEGATIVE REACTION ON 10 JULY. 1X

3. POINT III REPRESENTS A POSTSCRIPT TO WASHINGTON TELNO 1638. JAYCOX SAID THAT MCPHERSON WAS PERSONALLY COMMITTED TO FINDING A WAY FOR THE US TO PARTICIPATE. HIS CONFIRMATION AS DEPUTY SECRETARY TO THE TREASURY WAS EXPECTED IN TWO DAYS, AND HE SHOULD TAKE UP HIS POST BY END AUGUST. MCPHERSON'S OFFICE WAS WORKING ON A PLAN WHICH WOULD INVOLVE REFINANCING AND POSSIBLY SECURITISING THE RELEVANT EXPORT CREDITS. (COMMENT: WE WILL SEEK FURTHER DETAILS OF THESE IDEAS, BUT IT IS NOT CLEAR HOW THEY WOULD CIRCUMVENT THE CONGRESSIONAL AND BUDGETARY PROBLEM REFERRED TO IN TELNO 1638). 1Y

Restricted

/4.

COMMISSION OF THE EUROPEAN COMMUNITIES

COM(87) 320 final

Brussels, 5 August 1987

VERSION PROVISOIRE

Completion of the internal market:
approximation of indirect tax rates
and harmonization of indirect tax structure.
Global Communication from the Commission

COM(87) 320 final

harvest of prosperity of which they are intrinsically capable. Perhaps the starkest measure of the extent of the waste and of the urgency of the need for action is that, meanwhile, 16 million potential producers of wealth and growth stand unemployed. The simple truth is that we are failing to make use of the immense potential which Europe possesses.

What is the reason for this tragic waste of opportunity and potential? The Community's Heads of State and Government had long sensed that the answer lay in the disunity which still, nearly 30 years after the signing of the Treaty of Rome, marked the European economy itself. The countries of the European Community, for all their common heritage and common interest, remain a fragmented economy, divided into a dozen separate markets; each with its own rules; each manufacturing for its own market; each facing obstacles and difficulties in trying to trade with other Member States. That is why the Community has steadily fallen behind the more integrated markets of the United States and Japan in the growth of its demand, its production and its trade.

The Heads of State and Government, meeting in March 1985 in Brussels, set the target and the objective by identifying as their first priority "action to achieve a single large market by 1992 thereby creating a more favourable environment for stimulating enterprise, competition and trade; it called upon the Commission to draw up a detailed programme with a specific timetable before its next meeting".

The Commission's blueprint in response to this challenge was rapid, bold and radical. It has since been universally accepted as the foundation for a rebirth of European aspirations. The White Paper on completing the internal market did not mince its words:

"Europe stands at the cross-roads. We either go ahead - with resolution and determination - or we drop back into mediocrity. We can now either resolve to complete the integration of the economies of Europe; or through a lack of political will to face the immense problems involved, we can simply allow Europe to develop into no more than a free trade area.

The difference is crucial. A well-developed free trade area offers significant advantages: it is something much better than that which existed before the Treaty of Rome; better even than that which exists today. But it would fail and fail dismally to release the energies of the

COMPLETION OF THE INTERNAL MARKET: APPROXIMATION OF INDIRECT TAX RATES AND HARMONIZATION OF INDIRECT TAX STRUCTURES

GLOBAL COMMUNICATION FROM THE COMMISSION

1. Introduction: the economic and historical perspective

The Commission's White Paper on completing the internal market of the Community[1] was a response to the need to reverse the relative decline of western Europe. The undertaking is an ambitious one - to some perhaps frighteningly so - but it had to be ambitious if it was to measure up to the scale of what is needed. And the Governments of the Member States have firmly and repeatedly committed themselves to fulfilling those ambitions. They had already been searching for some time for a strategy - a strategy which would revive the entire economy of Europe and reverse the process of the previous decade or more which had caused our performance in terms of output to fall increasingly behind those of our main competitors in America and Japan.

Their recognition that the solution was to be found in the completion of the internal market goes back as far as the Copenhagen European Council in December 1982 and was reaffirmed at Dublin and Fontainebleau in 1984.

The Commission took up the challenge and gave it more concrete expression by declaring in the European Parliament in January 1985 that within 8 years - the life of two Commissions - a programme for the dismantlement of the Community's internal frontiers would be drawn up and implemented.

The population of the European Community is nearly half as large again as that of the United States and well over twice that of Japan. We are the biggest and oldest-established bloc of trading nations in the world. Our scientific knowledge and our capacity for invention are second to none. But for want of a dynamic regenerative impetus these immense resources in considerable measure lie fallow, failing to produce the growth and the rich

(1) COM(85) 310 final

regards the approximation of VAT and excise duties, the European Council invited the Council of Ministers for Financial Affairs (ECOFIN) to examine on the basis of the White Paper any measures which might be necessary for the achievement of a single market and the possible timetable for the application of those measures."

The ECOFIN Council delegated this mandate in the first instance to a high-level group of fiscal experts who, together with representatives of the Commission, considered the fiscal proposals outlined in the White Paper and the possible alternatives to it. The high-level group reported to the ECOFIN Council in June 1986 that the proposal would achieve the removal of formalities and fiscal controls at borders in the case of intra-Community trade and that the alternatives they had considered would fail to result in the removal of fiscal frontiers and could not, therefore, be recommended. Nevertheless, the report also made it clear that there were still considerable difficulties, uncertainties and hesitations, and concluded that "Member States will not be able to decide whether the measures envisaged by the Commission are ultimately acceptable to them until full details of the measures as a whole are available. Only when Member States can see clearly

- the financial, budgetary, economic and social consequences of the measures for them,

- the practical consequences for both the economy and individuals and the national budget entailed by the clearing mechanism,

will each of them be in a position to weigh up the advantages and disadvantages resulting from the Commission's system and decide whether it is prepared to agree to the system."

The ECOFIN Council in June 1986 discussed the group's conclusions and reserved its position until the Commission had submitted to the Council "detailed proposals on the rates and rate structure of indirect taxation and on the clearing system. On that basis the Member States will be able to state their position on the approach which the Commission envisages in Part III of the White Paper".

This Communication provides the detailed proposals for which ECOFIN have asked. It constitutes the beginning of the next, and probably most people of Europe; it would fail to deploy Europe's immense resources to the maximum advantage; and it would fail to satisfy the aspirations of the people of Europe."

The White Paper and its programme were welcomed and largely endorsed by the European Council meeting in Milan in June 1985. Six months later saw the adoption of the Single European Act which establishes as a legal commitment the objective of "an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured." A Europe without internal frontiers - not a Europe with fewer or simpler frontier controls, but one with no such divisive frontier controls at all. The programme in the White Paper is for a comprehensive elimination of all the barriers - the physical barriers, the technical barriers and the fiscal barriers - which cause the face of Europe to be scarred by the frontiers which divide it. One of the declarations that accompanied the Single European Act made specific reference to "decisions necessary to implement the Commission's programme described in the White Paper on the Internal Market".

The Commission and the Governments of the Member States are therefore firmly committed to embark on the completion of the programme.

2. Completing the Internal Market: the fiscal aspects

The Commission has taken as its starting point a snapshot of the existing wide spread of indirect tax rates and structures in the Community. It has then confined itself to setting out the minimum changes which must be made to that picture in order to achieve a sufficient degree of fiscal approximation. It must be clearly understood that the present package is not an attempt to design an ideal fiscal system for the Community, but a blueprint for abolition of fiscal frontiers. It is in that spirit that the Commission has tried to find the most practical possible solutions; and it is in that spirit, and taking possible problems of adjustment into account, that they are presented and must be studied. That is the job which the Commission was asked to do.

Already in Milan in June 1985, the European Council launched an intensive programme of activity based on the White Paper proposals. As far as the fiscal chapter (Part III) was concerned, the Milan conclusions stated: "As which fiscal approximation might impose on Member States' flexibility of response to be compensated for at a Community level.

All this, however, is yet to come. The immediate task for the Community is to study the proposals which accompany this communication and for each of its Members to evaluate their significance.

3. The Proposals

The White Paper demonstrated that if fiscal frontiers are to be abolished and the indirect taxation system of the Community is to serve the single unified market which we are committed to completing, there must be a considerable measure of approximation of indirect taxes. Only then, when indirect tax levels are sufficiently close as between one Member State and another so as not to distort competition and patterns of trade, will it be possible for the European economy to work in a free and unfettered way; only then will goods, services, capital and people be able to move freely to where they enjoy genuine comparative and competitive advantage. If we are to abolish the internal frontiers which at present divide us, it is vital to deal with fiscal frontiers and the underlying reasons for their existence. This is not a new dawning of the truth. It is something which has been accepted ever since the founding of the Community: and it has been re-affirmed on many subsequent occasions, not least in the Single European Act itself.

The abolition of fiscal frontiers will bring with it the abolition for intra-Community trade of the existing system of relieving goods from tax at export and of imposing tax at import, as has indeed been envisaged ever since the First VAT Directive was adopted twenty years ago. Elimination of the distinction made at present between supplies within a Member States and supplies to another Member State should result in significant administrative simplification for traders.

In addition, the removal of fiscal frontiers necessitates approximation of VAT and the main excise duties if unacceptable levels of distortion of competition, diversion of trade, and tax fraud are to be avoided.

The Commission is also proposing a VAT clearing mechanism to ensure that, after frontier controls have been abolished, the Member States continue to

decisive, phase of this dialogue. As is clear from the conclusions of the high-level group and the ECOFIN Council, the process of fiscal integration cannot begin in earnest until the Member States have had an opportunity to assess what fiscal approximation will mean to them in real terms. Only when a clear and coherent set of proposals for fiscal approximation is on the Council table will the Member States be in a position to weigh up the implications for themselves, and to determine what benefits and what costs they offer to each of them in their own particular circumstances, both in the shorter and the longer term.

Neither the Commission nor the Member States have ever had any illusion about the magnitude and the difficulty of the task ahead. But they have not hitherto been in a position to measure it. The present proposals are the basis on which that task of analysis, of evaluation and of eventual adjustment can now take place. Every effort will need to be made to find Community solutions to difficulties that may arise. If that should prove in some cases to be impossible, the Commission is prepared to examine with the Member States concerned what special measures might be applied to them. Such measures would have to be of a temporary nature and must cause the least possible disturbance to the functioning of the Common Market. The Commission could then propose appropriate solutions to the Council, notably as provided for in Article 8C of the Treaty as amended by the Single European Act.

As is discussed in more detail later in this paper, the path to abolition of fiscal frontiers in 1992 will be an easier one to tread for some Member States than for others. Some aspects may cause extreme difficulty in some cases, for example in Member States whose budgetary receipts would be significantly reduced or increased. The Community as a whole - the Member States and the Commission working together - will have to find ways, including the possibility of derogations where these can be justified, of easing the path for those of its members for whom the implementations of the proposals could pose political, social or budgetary problems. The proposals already provide a major element of flexibility; it is proposed that Member States be given freedom to determine their own path to 1992 and the pace at which they travel along it. The Council and the Commission will monitor the pattern of progress and may propose solutions to difficulties which manifest themselves. The Commission will consider the possibility of proposing complementary measures at a later date, which would enable the measures proposed here to be amended on a Community basis if economic developments were to make that desirable. This would enable any limitation consideration of the proposals. In what will be a challenging period of transition, the Commission has concentrated on two overriding priorities: its proposals must result in the best possible fiscal environment for economic operators in the internal market; at the same time they must minimize the adverse effects of the approximation exercise for Member States' revenue flows and budget flexibility. This document sets out in general terms the Commission's proposals for a manageable level of approximation. The specific proposals in question are listed in Annex A.

For ease of analysis, VAT and the excise duties are dealt with separately in the following two sections.

4. Approximation of VAT rates and rate structure

The First and Second VAT Directives, which laid down in 1967 the foundations of the Community VAT system, already clearly envisaged the abolition of tax on imports and the remission of tax on exports in trade between Member States and the approximation of legislation concerning turnover taxes in order to eliminate distortion of competition within the Community. This objective has been repeatedly confirmed over the years. Considerable progress has been made towards the creation of a common VAT base, notably with the adoption of the Sixth VAT Directive. The Sixth Directive lays down, in particular, a clear programme for the staged introduction of the fiscal conditions permitting the internal market to function. That programme is already under way. The Commission has put forward several proposals - notably the Seventh, Twelfth, Eighteenth and Nineteenth Draft Directives - designed to eliminate some of the most significant remaining areas of divergence. The Council should deal with these proposals as a matter of urgency. Certain derogations have not yet been tackled. More is said of these questions later in this Communication. Nonetheless, there now exists an identifiable common VAT base which represents a decisive step along the road towards a common fiscal system and thus towards the elimination of fiscal frontiers.

a) Number of rates

The starting point for any approach to the approximation of both the number and level of VAT rates must be the existing situation in the Member States. This is as follows:

receive the revenue to which they are entitled. It will ensure that output tax collected on export sales in one Member State is passed on to the Member States in which the supplies are finally consumed. The mechanism is described in detail in a separate Working Paper but is in essence a central account through which Member States will draw or pay money periodically, depending on the extent to which they are net importers or exporters. Member States will calculate the amount to be drawn from or paid to the central account on the basis of information supplied in traders' VAT returns. No additional records will need to be kept. For excise duties, no such system is needed, since these are not charged until the goods are released from bond, normally in the country in which they are to be sold to the final consumer.

There are, of course, other indirect taxes within the Community, such as taxes on the registration of vehicles, and on the purchase of houses, which vary considerably from Member State to Member State. Those variations can be such as to cause distortions of competition and deflection of trade. But they do not impede the free movement of goods in the sense that the differences between them do not give rise to controls or formalities at frontiers. The Commission actively pursues cases in which such indirect taxes breach the rules of the Treaty, but does not consider their approximation to be a necessary part of the abolition of fiscal frontiers.

In adopting its approach to the elimination of fiscal frontiers, based on the notion of the sufficient approximation of the existing patterns of indirect taxation in the Member States, the Commission is strictly implementing Article 99 of the Treaty as amended by the Single European Act. That Article calls for proposals "for the harmonisation of legislation concerning turnover taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is necessary to ensure the establishment and the functioning of the internal market within the time limit laid down in Article 8A (ie, 1992)". The Commission has refrained from proposing anything which is not strictly necessary for that purpose. There are pressures from one quarter or another to use the approximation process as a vehicle for achieving other fiscal changes or even non-fiscal policy objectives. The Commission considers, however, that it would not be justified in seeking to place additional strains of adaptation on Member States in this way. Every effort has been made to avoid running counter to other policy objectives, and to bear the wider economic social and regional implications in mind in formulating these proposals. But these are among the implications which can only be evaluated on the basis of a collective

The question of how many rates a Community multi-rate system should have is less clear cut. Whilst a majority of Member States have three or more rates, in practice they fall into two main camps, namely those with a standard and a reduced rate or rates and those with standard, reduced and increased rates. Taking into account the fact that, where Member States have more than three rates the more extreme rates normally apply to only a very limited number of products, the real choice lies between a two-rate and a three-rate system.

There is little doubt that a three-rate system creates more complications for both taxpayers and national administrations and that it would therefore be simpler and more cost-effective to move to a two-rate system than to oblige those Member States who currently do not apply an increased rate to move to a three-rate system. Furthermore, since the existing increased rates are applied to a relatively small proportion of the tax base in each Member State (on average below 10%), their abolition would not create undue budgetary problems. Finally, the coverage of existing increased rates is not particularly homogeneous and it would therefore be difficult objectively to draw up a common list of goods and services which should be subjected to an increased rate. For all these reasons, the Commission has concluded that a two-rate system would be preferable - namely a system with a standard rate and a reduced rate only.

b) Scope of the reduced rate

In most Member States the coverage of the reduced rate or rates is generally restricted to items of basic necessity. The zero-rates in Ireland and the United Kingdom cover much the same ground. Taking this into account, there is a considerable degree of consistency in the different Member States. The Commission proposes therefore that the following basic goods and services should be taxed at a reduced rate under the harmonized Community VAT structure, **but it is important to read this list in conjunction with what is said at 2d) below about zero rates.**

- foodstuffs (with the exception of alcoholic drinks);
- energy products for heating and lighting;

	Reduced Rates	Standard rate	Increased rate
Belgium (1) (2)	1 & 6	19	25 & 25+8
Denmark (1)	-	22	-
France	2.1; 4 5.5 & 7	18.60	33 1/3
Germany	7	14	-
Greece	6	18	36
Ireland (1)	2.4 & 10	25	-
Italy (1)	2 & 9	18	38
Luxembourg	3 & 6	12	-
Netherlands	6	20	-
Portugal (1)	8	16	30
Spain	6	12	33
United Kingdom (1)	-	15	-

Rates applicable as at 1.4.1987

From the above it can be seen that all Member States, with the exception of Denmark and the UK, apply more than one rate. Thus, although the Commission accepts that, in theory, a VAT system with only one rate is the simplest and most efficient structure, it is clear that such an approach would have disruptive consequences for all Member States, other than the two mentioned, and is unlikely to be acceptable to the Community as a whole. It is therefore proposed that a multi-rate system should be adopted.

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(1) Also applies an exemption with a right to refund (ie a zero-rate) to certain domestic transactions (NB all Member States apply the zero rate for exports and like transactions).

(2) Also applies an intermediate rate of 17%

Turning to the reduced rates, these currently vary from 1% to 10% but the lowest rates apply only to a very few products and those with significant coverage vary from 4% to 10%. On the other hand, it also has to be borne in mind that two Member States currently apply a zero rate to most, if not all of the basic goods and services which are included in the list of items to be taxed at the reduced rate. Taking these various factors into account, the Commission has concluded that the permitted range for the reduced rate should be between 4% and 9% though in view of the inclusion in this rate band of certain sensitive sectors, such as the cultural sector, the Commission recommends that Member States fix their rate in the lower half of that band.

The weighted average VAT burden resulting from these calculations (i.e. the total tax yield in proportion to the total harmonized tax base) in the Community is currently around 13%. The proposed rate bands will permit Member States to choose rates which will result in a minimum of disruption for the maximum number of Member States in terms of this existing tax burden. The future weighted average VAT burden will, of course, depend on the actual choices made by the Member States within the permitted bands.

d) Derogations, zero rates and exemptions

The White Paper acknowledged that some countries would face considerable difficulties with fiscal approximation; and it said that derogations might be needed to meet these problems. This is likely to be of particular importance in the case of zero rating.

It has always been an accepted part of Community policy that zero rating, except in the case of exports, was a temporary measure which would disappear with the Completion of the Internal Market. This was clearly stated in the second VAT Directive adopted in 1967 and restated in the Sixth VAT Directive adopted in 1977.

The zero rating of supplies generally acknowledged as basic necessities rests upon considerations of social policy; though it is clearly a less efficient way of achieving such objectives than measures more

- supplies of water;
- pharmaceutical products;
- books, newspapers and periodicals;
- passenger transport.

Overall, these items represent approximately one third of the common Community tax base.

c) Rate levels

The standard rates currently applied in the Member States vary from 12% (Spain and Luxembourg) to 25% (Ireland). This is clearly too wide a band to permit the abolition of fiscal frontiers without serious economic consequences. The spread of rates therefore has to be narrowed to a point where the difference between the upper and lower limits will itself not create intolerable price differences between the Member States (especially those which are adjacent). On the other hand, the Commission is conscious that the narrower the band becomes, the greater is the number of Member States that will suffer budgetary disruption. In terms of the second of these criteria, the optimum spread of the standard rate band would be 8 points (which would incorporate 10 out of the 12 standard rates currently applied, within a band from 12% to 20%). Unfortunately, however, neighbouring Member States are to be found at either end of this spectrum and the Commission has been forced to conclude that the resulting tax-induced border price differentials would generate trade distortions and fiscal fraud, which Member States would be likely to find unacceptable.

If, however, the standard rate band were narrowed from 8 to 6 points there would still be 8 Member States who would currently fall within this range (if the parameters were set at 14% and 20%) and the resulting price differentials would become that much less distortive and more manageable. The Commission has, therefore, concluded that the optimum norm for the standard rate should be within a permitted range of between 14% and 20%. In fixing their own individual rate within this band, Member States would need to take into account the effect of market forces once fiscal frontiers had been eliminated - and would, of course, be entirely free to do so.

part in the discussion of any derogations for which Member States in real difficulty might feel the need. But that dialogue cannot commence until the present proposals have been studied and evaluated by all concerned.

This is not the place to deploy at any length the arguments for and against such derogations. The principle which needs to be respected all the time is the integrity of the Internal Market. Clearly where trade between Member States inevitably involves significant additional costs, it may well be possible for the market to accommodate cost differences resulting from derogations without too much risk of deflection or distortion of trade. But where cross-border shopping is easy and involves' of itself no significant additional costs, derogations might well create significant distortions. For this reason also derogations are not simply a matter concerning the Member States asking for the derogation, but concern also the other Member States.

The second point which needs to be made is that derogations always carry a cost - which ultimately is borne primarily by the Member State concerned. The objective of the Completion of the Internal Market is to reduce actual and identifiable costs arising from the present frontier controls, and to give industry a more cost-effective basis on which to conduct its operations by having access to an undivided market of 320 million instead of primarily to its own domestic market only. Derogations may well lead neighbouring Member States to insist on the maintenance of frontier controls directed specifically against the Member State concerned. It would be a tragedy for the Community as a whole and in particular for the Member State concerned if by its own policies it forced itself into a position where effectively it had cut itself off from the overwhelming benefits which will flow from the integrated European market.

A word should also be said here about exemptions. The Sixth VAT Directive, in laying down the basic principles of the tax base, designated certain supplies as in principle exempt but gave Member States the option to continue to tax some of them on a transitional basis. Others were to be in principle taxable, but again as a transitional measure, Member States were allowed to continue to exempt closely targeted towards those in need. Only two Member States have followed such policies to any significant degree; the other Member States have successfully accommodated themselves to a broadly based concept of VAT without the extensive use of zero rating. This has been achieved by direct compensation of disadvantaged groups through the social security system and welfare payments, thus directly benefiting the groups primarily affected in a more cost-effective way than is achieved by a fiscal price subsidy. It should also be remembered that zero rating, by giving a price advantage to the products of one Member State, distorts competition within the Community; this is particularly true when applied to supplies which feed through into industrial and commercial costs. Finally, it needs to be remembered that, for any given yield of revenue, zero rating in one area must inevitably lead to a higher overall rate of tax elsewhere; if 50% of consumer expenditure is exempted by zero rating, the rate of tax elsewhere necessarily has to be twice what it would have been if there had been comprehensive coverage.

For all of these reasons, the Commission could not recommend that the Community should abandon what has been its considered and settled policy ever since the VAT was first adopted. It is for this reason, that in the rates and coverage proposed above, the Commission has not proposed zero rates, but has proposed that for the most part basic necessities should be charged at the reduced rate, as is the practice in almost all the Member States.

Nevertheless, the Commission accepts that some Member States face difficulties. The Commission recognises that the Member States concerned may well wish to be granted derogations to meet their particular difficulties. Indeed, this point was clearly recognised in the White Paper itself.

The Commission has indeed considered whether it should already at this juncture propose such derogations but has come to the clear view that it would not in any event be practicable to do so until the Member States have had a chance to study its proposals and consider what particular difficulties they may present. Though the proliferation of derogations would present serious problems that could threaten the operation of the internal market and the objective of abolishing fiscal frontiers, the Commission would of course take a constructive importance for Member States' budgets. For tobacco products, where the Commission is proposing a composite rate for the ad-valorem excise duty and VAT, taken together, a margin of flexibility is proposed which is equivalent in its effect on retail prices to the margin proposed for VAT on other goods. More generally the possibility of providing a margin of flexibility on excise duties in particular cases of difficulty would depend on whether it was compatible with the objective of the abolition of frontier controls.

As regards the level of excise rates, the present divergence between Member States is much greater than in the case of VAT and it is consequently that much more difficult to arrive at an optimal solution which will cause the least amount of disturbance to the greatest number of Member States. Account must also be taken of other Community policies which affect mineral oils, tobacco products and alcoholic beverages.

In determining the rates the Commission's general approach has been to secure equity between Member States and the minimum disruption in each sector. The method for achieving this has varied according to the particular circumstances or characteristics of each sector in question.

Accordingly, in the case of tobacco products the rates have been calculated on the basis of the Community arithmetic average which gives equal weight to the rates applied by each Member State. The resulting rate produces an increase in the overall taxation of manufactured tobacco at Community level, which is consistent with the Commission's policy in health matters, set out in the report to Parliament in 1982 (COM(82)61 final) and in the Action Programme: "Europe Against Cancer" (COM(86)717 final).

The alcoholic drinks sector is broadly composed of two categories - distilled and fermented beverages. For the former (ie spirits) the Commission has taken the Community arithmetic average. However in the case of the fermented beverages (wine and beer) it was found that the effect of the arithmetic average, and also of an average weighted by consumption, would be highly disruptive. The solution proposed for these products, which are in competition, is therefore to tax them equally per litre of product on an overall revenue-neutral basis.

them. The draft Eighteenth VAT Directive, still before the Council, seeks in the interests of fair competition within a single internal market to bring many of these transitional options to an end - either as permanent exemptions or by bringing the supplies concerned definitively into the tax net; others remain to be settled at a later stage, including the treatment of gold (other than for industrial use) and of works of art, where further thought needs to be given to what the definitive régime should be. Further proposals will therefore be needed, as foreseen in White Paper programme.

5. Excise duties

When first putting forward its proposals in 1972 for harmonizing the structures of excise duties, the Commission singled out for retention and harmonization at Community level the excises on manufactured tobacco, mineral oils, spirits, wine and beer. The other excise duties were to be phased out to the extent that they involved tax adjustments at internal frontiers. This programme had as its ultimate objective the creation of conditions permitting the abolition of fiscal frontiers.

This objective can, of course, only be met when common rates of excise duty are charged on harmonized structures throughout the Community. The present proposals, put forward under the White Paper programme, complete the process by laying down the common rates to be applied to those structures. It should be stressed, however, that very little progress has so far been made in the Council towards the adoption of the Commission's structural proposals. Consequently, the considerations in respect of the excise duties are more complicated than those in respect of VAT because not only the rates but also the structures still differ widely between different Member States.

As far as excise duties are concerned, any flexibility in the rates of duty which might be permitted would be compounded with the permitted margin for VAT rates and would therefore result in tax-induced price differentials well in excess of 6%. This is because VAT is imposed on the price of goods inclusive of excise duty. Consequently, the Commission has proposed that, as a general rule, any margin of flexibility in approximating rates should be reserved for the VAT rates because these rates have by far the widest coverage and therefore have an overriding

Mineral oils

Petrol, leaded, and medium oils used as propellants, per 1000 l	340 ECU
Petrol, unleaded per 1000 l	310 ECU
Liquified petroleum gas (LPG) per 1000 l	85 ECU
Diesel (gas-oil) per 1000 l	177 ECU
Heating gas-oil and medium oils used as fuels other than propellants per 1000 l	50 ECU
Heavy fuel oil per 1000 kg	17 ECU

It should be noted that the excise duties proposed above are based on the situation as at 1 April 1987. Between now and 1992 the amounts of the specific duties will be adapted annually by the Commission in accordance with the general consumer price index in the Community and the revised figures will be communicated to the Member States.

6. Overall budgetary effects

As indicated previously, the Commission has kept in mind in formulating its proposals the need to minimize budgetary disturbance for the maximum number of Member States.

While the eventual adjustments which may be needed in individual Member States' budgetary arrangements are primarily and properly a matter for the Member States concerned, some tentative global qualitative assessment of the likely overall effects of the Commission's proposals can be given at this stage. Any quantitative estimates would have to be based on purely mechanical calculations which could not take account of the effects of changes in demand which tax and price changes may generate (elasticity effects); or of the effects on frontier trade; or of any macroeconomic stabilising mechanisms which may operate in the absence of

For mineral oils the Commission is proposing, for each main category of product, a rate which minimises disturbance to national tax revenues or industrial cost patterns. Thus for petrol which is by far the most important producer of revenue in this sector, a rate based on the arithmetic average of existing rates has been chosen. For diesel, heating gas oil and heavy fuel oil on the other hand, whose use is predominantly commercial, the Commission considers that an average weighted by consumption would be more appropriate, as it minimizes the effects on industrial costs.

On the basis of these considerations the Commission accordingly proposes the following rates:

<u>Alcoholic drinks</u>	<u>Amounts in ECU</u>
Alcohol for beverages (per hl of pure alcohol)	1271
Intermediate products (per hl)	85
Wine (per hl) average 11% vol)	17
Beer (per hl) (average 12,5° plato)	17
<u>Manufactured tobaccos</u>	
Cigarettes (specific excise per 1000)	19.5
ad val + VAT (in % of retail price)	52%-54%
Cigars and cigarillos ad val + VAT (in % of retail price)	34%-36%
Smoking tobacco ad val + VAT (in % of retail price)	54%-56%
Other manufactured tobacco ad val + VAT (in % of retail price)	41%-43%

being made by the Member States and will report periodically to the Council, in accordance with the provisions of Article 8B of the Treaty as amended by the Single European Act. Such reports will consider the need for proposals for any complementary amending measures to take account of economic developments.
Furthermore, the Commission is putting forward a Convergence Proposal which replaces the standstill proposal currently before the Council (1). The convergence proposal, which covers both the VAT rates and the main excise duty rates, aims to ensure that Member States do not diverge from the overall objective in the meantime.

8. Conclusions

The abolition of fiscal frontiers is a vital element in the completion of the internal market. But it will also be an achievement of incalculable value in itself. The most direct and immediate benefit would accrue to industry and commerce as the administrative cost of fiscal frontier formalities virtually disappeared and the time spent in transporting goods was reduced. Relieved of those costs, firms in the Community would become more price-competitive both within the internal market and internationally. That in itself would increase their potential market and lead to economies of scale in production. These, together with the reduction in administrative costs, would be reflected in lower prices for the consumer. Real domestic demand in the Community would rise, with favourable effects on GDP growth. And, of course, the cost of frontier controls to member governments would be reduced. Frontier controls for fiscal reasons constitute the overwhelming majority of such controls. A Community in which it was no longer necessary for the citizen to worry about whether or not he had exceeded his travellers' allowance or whether he could drive his car into one Member State or another; a Community in which traders could do business with customers in other Member States just as they do with customers in the next street or the next town; a Community in which there would no longer be the endless queueing and form-filling and rubber-stamping at frontier posts; a Community in which goods and services no longer bore the extra and unnecessary cost of delay and bureaucracy; such a Community is well worth the effort on all sides that the Commission's proposals will undoubtedly require.

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(1) COM(85) 606 as amended by COM(87) 17

compensatory measures. Taking such effects into account would in principle reduce the initial budgetary gains or losses shown. The Commission is, however, very conscious that in view of the complexity of the present tax rates and structures, and in view of the freedom given to the Member States to determine how they make the fiscal changes they need between now and 31 December 1992, any quantitative estimate of these moderating effects would be particularly difficult and unreliable. In particular an in-depth study of such effects would require a prior knowledge of the nature and extent of any compensatory policies which the Member States might adopt, depending on their budgetary situation and the use they make of indirect taxation. The Commission asked for such information early on in the process of formulating its proposals but has had only an inadequate response. The task of evaluating the effects of these proposals for individual Member States is, in any case, primarily a task for the Member States themselves. With the publication of the proposals, that is a task on which they can now begin. The Commission has already undertaken a certain amount of exploratory work in collaboration with national administrations. It is ready to pursue these studies and to complete them on the basis of any suggestions which the Member States may submit as to the adjustments they may consider desirable.

Subject to these qualifications, it seems probable that three Member States (Belgium, Italy, the Netherlands) would be able to continue to obtain the same level of total tax revenue from the VAT and excise duty rates proposed as they currently receive. One Member State (France) would suffer a slight budgetary loss, while three Member States (Germany, United Kingdom and Greece) would obtain small or moderate increases in budgetary receipts. Two Member States (Ireland and Denmark) would suffer pronounced budgetary losses, while the other Member States (Luxembourg, Spain and Portugal) would obtain substantial increases in budgetary receipts.

7. Timetable

It is intended that Community rates for VAT and the excise duties should enter into force no later than 31 December 1992. It will be the responsibility of the individual Member States to work towards these rates in the intervening period. The Commission will monitor the progress

ANNEX A

PROPOSALS TO BE SUBMITTED IN CONNECTION WITH THE APPROXIMATION OF INDIRECT TAX RATES AND HARMONIZATION OF INDIRECT TAX STRUCTURES

A) VAT

1) Proposal for a Council Directive supplementing the Common System of Value Added Tax and amending Directive 77/388/EEC - approximation of VAT rates. COM(87) 321

2) Proposal for a Council Directive supplementing the Common System of Value Added Tax and amending Directive 77/388/EEC - Abolition of Fiscal Frontiers. COM(87) 322

3) Outline Working Paper for a Community VAT clearing mechanism. COM(87) 323

4) Proposal for a Council Directive instituting a process of convergence of rates of value added tax and excise duties. COM(87) 324

B) EXCISES

1) Proposal for a Council Directive concerning the approximation of taxes on cigarettes. COM(87) 325

2) Proposal for a Council Directive concerning the approximation of taxes on manufactured tobacco other than cigarettes. COM(87) 326

3) Proposal for a Council Directive concerning approximation of the rates of excise duty on mineral oils. COM(87) 327

4) Proposal for a Council Directive concerning approximation of the rates of excise duty on alcoholic beverages and on the alcohol contained in other products. COM(87) 328

That effort, the Commission acknowledges, will be a considerable one. The Commission has done as much as possible to minimise it, but is nevertheless well aware that for some Member States the measures proposed will create problems, even though they allow a degree of flexibility and a reasonable period for adjustment (i.e., until the end of 1992). The Commission has, therefore, always acknowledged that there may be a need for derogations since these difficulties cannot be allowed to jeopardize the fundamental objective of creating a single European market. Nevertheless, it is in the general interests of the Community that such derogations should be kept to the minimum.

The Commission is nonetheless convinced that the present proposals for the approximation of the VAT and excise rates, taken in conjunction with the proposals already on the table, will serve two major purposes. They will firstly permit the abolition of fiscal frontiers; they will thus contribute towards the attainment of an integrated and expanding European economy. They will also satisfy, so far as possible, the legitimate concern of individual Member States that their existing economic and taxation systems should not be unduly disrupted.

FUTURE FINANCING

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FUTURE FINANCING: PRESENT POSITION AND LIKELY COURSE OF THE NEGOTIATIONS

This note summarises where we have got to in the ex novo review of the Community's financing arrangements, and discusses briefly the timetable for negotiations during the rest of the year.

The European Council

2. The Brussels European Council on 29/30 June considered all the main elements in the future financing dossier: improved budget discipline and management, reform of the CAP, the increase in the own resources ceiling, more effective use of the structural funds, and the UK's budget imbalances mechanism.

3. The Council could not really be described as a success. Although there was considerable agreement on the steps to be taken to resolve the main problems, the UK could not agree:

(i) that there should be discussion at that stage on the size of any increase in the own resources ceiling. Before that question could be addressed, agreement was needed on effective and binding controls over Community spending, particularly agricultural spending;

(ii) that the level from which we start to calculate the agricultural guideline should include <u>all</u> the 1987 overrun.

4. The text of the Council conclusions agreed by the eleven was helpful insofar as it said that:

- the use of the Community's resources should be subject to effective and binding budget discipline;
- additional measures were required to stop surplus agricultural production, and so reduce costs and keep

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expenditure within the budget framework.

One interesting point is that the conclusions refer to the need to express the new own resources ceiling as a fixed percentage of Community GNP.

5. One unhelpful point is that they can be interpreted as saying that structural fund expenditure should grow faster than the maximum rate.

The Commission's five papers

6. Since the European Council, the Commission have produced five papers on future financing issues.

7. The first of these is a draft new own resources decision (COM(87)420). This incorporates the Commission's proposals on own resources, including a new own resources ceiling of 1.4 per cent of Community GNP, annual sub-ceilings (rising from 1.2 per cent of GNP in 1988 to 1.3 per cent in 1992), the introduction of the diff tax, a 1 per cent ceiling on VAT, the abolition of own resources refunds, and the conversion of customs duties on coal and steel imports into own resources. The draft ORD does not refer to the UK's abatement mechanism so as not to prejudice future discussion on this topic.

8. There are no real surprises here. Our main concern over the months ahead will be to limit the increases in the own resources ceiling and to ensure that whatever abatement mechanism is agreed leaves us at least as well off as we are under the Fontainebleau financing arrangements.

9. The Commission's communication on agricultural reform (COM(87)410) reviews past agricultural reforms, proposes new automatic stabilisers for each of the main commodity regimes, and outlines a policy for preserving the structure of European agriculture. The section on automatic stabilisers is considerably more helpful than it might have been (and represents a welcome response to UK pressure in this area), though we shall still need to tighten up the proposals in certain areas. The key thing, of course, will be to convince other member states that radical

reform really is essential.

10. The Commission's communication on budget discipline (COM(87)430) contains little that is new. As far as agricultural spending is concerned, the call for new automatic stabilisers and the plea for agricultural spending to be kept within the financial guideline are helpful. But the definition of the agricultural guideline is still not water-tight (because, for example, too much is allowed for exceptional circumstances and exchange rate movements), and the Commission are still wedded to the idea that the guideline should take account of the full amount of the 1987 overrun.

11. The proposals for containing DNO expenditure are no better than those put forward previously. Far too much reliance is placed on the possibility of restricting expenditure by having an inter-institutional agreement between the Council and the Parliament at the beginning of the budgetary procedure, and on the part to be played by the Commission's multi-annual forecasts. In general, the Commission's proposals on DNO represent a weakening of the budget discipline arrangements agreed at Fontainebleau.

12. The Commission's communication on the structural funds (COM(87)376) covers a draft framework regulation incorporating the main elements in the Commission's proposals set out in COM(87)100 and 101. The Commission calls for a doubling of structural fund commitments in real terms by 1992. It argues that the funds should be targeted more effectively, and that upto 80 per cent of the regional fund should be devoted to assisting backward regions. Over the coming months, we shall want to secure agreement to a much lower growth of total structural fund expenditure (notwithstanding what was said in the Brussels European Council conclusions), but with a rather higher proportion of that expenditure devoted to regions suffering industrial decline.

13. The Commission's revised draft financial regulation (COM(87)400) provides for the Commission's main proposals on budget management and for a permanent switch from advances to

reimbursement of agricultural expenditure. Although the budget management proposals represent a step in the right direction (eg by restricting carry-forwards so as to reinforce the annuality principle of Community expenditure), they do not go far enough. For example, the draft regulation denies the Council the last word on carry-forwards, and ignores entirely our concerns about "action ponctuelle". It also provides for a general budgetary reserve, to which we are opposed.

Timetable for future discussions

14. At working level, the main forum for further discussion will be the special COREPERs. Nine meetings are planned between 7 September and 17 November. Attention will be focused initially on budget discipline, the structural funds and the new own resources decision. Other official level working groups will take a first look at agricultural reform, the revised draft financial regulation and (possibly) the structural fund framework regulation.

15. At ministerial level, the key dates are as follows:

- 10 September: PMG to meet Christophersen
- 11 September: PMG to meet Danish budget minister
- 11-13 September: informal ECOFIN
- 14-15 September: FAC
- 21-22 September: Agriculture Council
- 18 September: PM to meet Goria
- 23 September: PM to meet Danish PM
- 24-25 September: PM to meet Kohl
- 1 October: OD(E) on future financing
- 3-4 October: informal FAC
- 12 October: ECOFIN
- 19-20 October: FAC
- 19-20 October: Agriculture Council
- 16 November: ECOFIN
- 16-17 November: Agriculture Council
- 23-24 November: FAC
- early December: possibility of FAC conclave
- 4-5 December: Copenhagen European Council.

16. At present, future financing does not feature on the agenda of any of the ECOFIN meetings. The Agriculture Council has been asked to look at the "specifically agricultural elements" of budget discipline. They will need to work quickly. The Presidency have expressed the view that, if there is to be a chance of an agreement at the European Council, the Agriculture Council will need to reach decisions on agricultural stabilisers and some other difficult issues at the meeting of the Council on 19/20 October (in practice, there might be scope for a little slippage, but not much). The Presidency will want to submit a report on future financing questions to the European Council. This report will need to be finalised at, or immediately following, the FAC meeting on 23/24 November.

UK objectives

17. Our main objectives will be:

(i) to limit the increase in the own resources ceiling to a defensible level;

(ii) to reach a good settlement on budget discipline. It will be particularly important to reach agreement on effective automatic stabilisers to limit agricultural expenditure on specific regimes. We also want to secure agreement on the lowest realistic figure on which to base the agricultural guideline and on effective means for ensuring that it is respected in practice;

(iii) to ensure that, overall, the new financing arrangements and corrective mechanism leave the UK at least as well off (and preferably better off) than with the continuation of the Fontainebleau arrangements.

INSURANCE UNDER DANISH PRES

J

INFORMAL ECOFIN 11-13 SEPTEMBER 1987 — ANNEX J

COUNCIL DISCUSSION ON INSURANCE UNDER THE DANISH PRESIDENCY

Attached are:

(1) EC's submission of 1 September

(2) Ms Ryding's minute of 2 September

August 13, 1987

THE MINISTER OF FINANCE AND
THE MINISTER OF ECONOMIC AFFAIRS
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DK-1216 Copenhagen K
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PWP

~~Alex~~ OTR

Jonathan/ov.

Mr. Nigel Lawson
Chancellor of the Exchequer
Parliament Street
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England

* = ITEM 2 ONLY. 17/8

CH/EXCHEQUER	
REC.	17 AUG 1987
ACTION	SIR G. LITTLER
COPIES TO	SIR P MIDDLETON MR H.P. EVANS* MR MOUNTFIELD* MR PERETZ MR KELLY MR WALSH* MS. LIFE*

Dear Colleague,

We enclose two notes, that we have received from the President of the Commission for the informal ECOFIN meeting in Nyborg September 12, relating to respectively item 1 and 2 on the agenda.

With best regards

Palle Simonsen

Anders Andersen

COMMISSION
OF THE
EUROPEAN COMMUNITIES

The President

Brussels, 30 July 1987

Confidential

The Complete Liberalisation of Capital Movements and Strengthening the EMS

I. Introduction

The Community has set itself the goal of completing the internal market in which goods, persons, services and capital will move freely by 1992. In May 1986 the Council adopted a communication from the Commission which presented a programme for the liberalisation of capital movements in the Community. The first stage of that programme resulted in the enactment of a Directive in November 1986 which came into force in February 1987. Already some of the Member States concerned have gone further than required by this Directive, and a number of Member States have removed all restrictions on capital movements. The complete freedom of capital movements should be possible among a majority of Member States, before the 1992 target date.

The final stage of the liberalisation of capital movements will take place against a background of a rapidly changing international financial system. The volume, volatility and velocity of financial transactions has increased enormously over the last few years despite the disappointing performance of the world economy. Financial transactions have become increasingly disassociated from the real economy; and at the same time there have been unprecedently large external imbalances between countries and huge swings in real exchange rates. There has been an increase in systemic volatility and fragility. Furthermore, financial and technological innovation, as well as some significant policy changes have led to a globalisation of financial markets, with the result that the number of cross-border and cross-currency transactions is increasing at least as fast as financial activity within any one country. More attention should be given to the potential risks associated with this situation.

The final stage of the liberalisation of capital movements within the Community, which is only one element in the process of creating an integrated financial market, will not add significantly to the risks which are associated with these overall developments, but it should not be undertaken without using the opportunity to minimise those risks.

The strategy should neither be to resist inevitable changes nor to opt for wholesale deregulation; instead it is necessary to manage change. Further liberalisation of capital movements will in most cases reinforce the dynamic process through which the financial systems in the Member States will fuse together; but uncontrolled, this process could lead to a gradual drift towards a lowering of prudential standards, through a competition in laxity. Those nations with the most stringent regulation and supervision would be under pressure from their financial institutions, whose costs must partly reflect these rules, to relax controls. To achieve a balance with the interest of the users of financial services, the Commission has proposed a comprehensive programme which will ensure a sufficient degree of harmonisation of regulation of financial services so that all Community countries can have confidence in each other's systems. The needs of the internal market and the EMS require that these risks are treated at a Community as well as a world level.

Special transition measures will have to be made for the minority of members whose financial systems do not allow them to proceed as quickly as the others with capital liberalisation. The arrangements would include a binding time-table; and in some cases there could be Community assistance. The Commission has already announced its plan to broaden the scope of the Community instruments which provide medium-term balance of payments assistance. In the past these instruments have been activated to assist members which have introduced or tightened exchange controls at a time of a balance of payments crisis. It is now proposed that their use could be extended, with the appropriate conditionality, to support a Member State which is moving towards further liberalisation of capital movements, despite a difficult external position.

Further liberalisation of capital movements has far-reaching implications for the EMS, which must in any case be strengthened in the light of recent experiences and of developments in the international system. On the one hand increased capital mobility will reinforce the external constraint which already exists on exchange and interest rate management for all Member States. On the other hand it increases the potential for destabilising capital flows and market volatility. To ensure that increased exchange rate instability does not undermine the progress towards the ultimate objectives of monetary stability and the achievement of a unified market that has already been made, it is necessary to increase the co-ordination of monetary policy through a strengthened EMS.

II. Scope of the next stage

The next stage of liberalisation of capital movements will also be the final stage. Innovation has already eroded the barriers between markets to such an extent that it is not possible to make any differentiation between transactions to be liberalised in the next stage. It will also involve more than the removal of exchange controls. Restrictions and distortions which prevent the effective exercise of the liberty to transfer capital, must also be removed, in conformity both with recent rulings of the Court of Justice and with Article 67 of the Treaty, which states that the Member States shall progressively abolish between themselves all restrictions on the movement of capital belonging to persons resident in Member States.

It is this formulation which will form the basis of the Directive that the Commission intends to present shortly to the Council. The proposed new Directive will contain a specific safeguard clause which will permit the reimposition of exchange controls, on a temporary basis and under Community supervision, for monetary transactions if the national authorities consider that their policies are threatened by sharp disturbances.

The purpose of the final stage of liberalisation of capital movements is to ensure that residents in liberalising Member States are effectively and fully entitled to benefit from the opportunities offered in the financial markets in other Member States.

In practice, as the removal of restrictions will be made "erga omnes", they will also be entitled to benefit from the opportunities offered by all other financial markets. This however will not be a provision in the proposed new Community texts. The 1972 Directive on regulating international capital flows and neutralising their undesirable effects on domestic liquidity, which ensures that Member States possess the necessary instruments for activating the safeguard clause referred to above should be modified to enlarge the scope of the instruments and make their use more symetric. It could also be modified to provide a further legal basis for the co-ordination of external policy to allow for a concerted implementation of protective and/or monetary policy instruments in order to regulate short-term capital movements to or from third countries.

II.1 Prudential supervision

Given the high level of prudential supervision that is present in all Member States, further harmonisation is not a precondition for the full liberalisation of capital movements. Increased capital mobility will not endanger their financial systems, it will however increase the need for a minimum degree of harmonisation to ensure both the conditions for fair competition between financial intermediaries and the protection of investors and savers.

A fully integrated Community-wide financial area will involve the free movement of financial services as well as the complete liberation of capital movements. The legislative proposals in the White Paper on the internal market lay out the Commission's views on what will provide the necessary basis for the liberation of financial services. The approach followed is to identify the minimum harmonization of essential prudential and supervisory standards required to underpin the mutual recognition of standards and thus the principle of home country control. It should be emphasised that minimum harmonisation does not mean harmonisation at a minimum level. The Community must offer a high level of protection which also takes into account the general need to adapt Member States' legislation governing banking and securities markets to the changing environment; and consider the interests of the European financial services industry in the global market-place.

Depositors and investors will continue to be protected by their own national regulatory and supervisory systems for the financial transactions that they make in their country of residence. Liberalisation of capital movements will however give them an extra degree of choice and should as a rule give greater freedom of access to the financial services offered in other Community countries or indeed the rest of the world. In exercising this choice, they naturally put themselves under the prudential regime of that other country.

II.2 Fiscal questions

In some Member States the domestic financial system is extensively used for the purposes of control and collection of taxes, especially those on investment income and capital gains. Although it should be noted that those states which have already fully liberalised have satisfactorily coped with fiscal problems, and that it is not the absence or presence of exchange controls which determines the amount of fiscal evasion, the Community cannot be indifferent to this concern. For the case of dividend income the Commission's proposals for the harmonisation of corporate taxation include harmonisation of corporate tax systems on a partial imputation model and a provision for a common level of withholding tax. For the case of interest income from deposit accounts and bonds, for which a common withholding tax is unlikely to be acceptable, the solution lies in an enhanced coordination between national authorities, based in part on the 1977 Directive concerning mutual assistance between national authorities over direct taxation, which allows for information to be exchanged where fraud is suspected.

As well as ensuring that the full liberalisation of capital movements does not lead to an increase in fiscal evasion, it is also necessary to ensure that provisions in national fiscal regimes do not constitute a disincentive to capital movements. There are a number of schemes in various Member States which by discriminating in favour of domestic securities effectively impede the free movement of capital. These will have to be progressively removed.

III. Strengthening the EMS

To reap the full benefits of an integrated financial area which include : a more efficient allocation of financial resources; lower costs and wider choice for individual and business consumers of financial services; deeper and broader markets; and a more dynamic European financial industry which should be better able to compete world-wide, will also require continued monetary stability through a strengthened EMS.

The international situation, which combines substantial overshooting and extreme volatility of exchange rates and massive payments imbalances, clearly demonstrates the inconveniences of combining increased capital mobility with a lack of monetary order. Experience has shown that floating exchange rates do not allow different countries to pursue their national policies independently. There are no techniques that allow countries both to insulate themselves from the rest of the world and to capture the gains that are potentially available from increased trade and higher levels of interdependence. Nor is it sufficient that individual countries independently pursue stability oriented policies. Certainly that is necessary, but international stability also requires co-operation and co-ordination, as is now generally accepted. Indeed a great deal of progress has been made, especially since the Tokyo summit of May 1986.

The international monetary system is in some important respects, tending towards a direction which the Community already took in 1979 with the setting up of the EMS. Further liberalisation of capital movements however reinforces the need to strengthen the EMS. By allowing increased mobility of short-term and monetary assets, the final phase increases the potential for destabilising speculative flows which could jeopardise the achievements that have been made with regard to price and exchange rate stability.

The System must be strengthened in such a way as to minimise the possibilities that such flows will in practice materialise, and to ensure that their potentially harmful effects can be attenuated as much as possible.

A balanced approach, relying on both tighter policy co-ordination and strengthening the system's mechanisms will be necessary for three principal reasons. First, it is accepted at a theoretical level that if a group of countries have both fixed exchange rates and completely free capital movements between themselves, there would be no scope for separate national monetary policies. As the EMS is not a fixed rate system, some flexibility at each of the points of the triangle composed of : mobility of capital movements, exchange rate stability and unity of monetary policy, is vital. Second, policy co-ordination, although a key ingredient to overall success, cannot in itself eliminate the possibility of destabilising capital flows triggered by non-policy or external shocks. Finally it is essential to complement increased capital mobility and the progressive creation of a unified financial market by strengthening the system's mechanisms in such a way as to ensure a reasonable degree of symmetry.

III.1 Policy co-ordination and indicators

Macro-economic indicators can help to strengthen policy co-ordination both through making the surveillance process more concrete, and by providing a detailed and quantified view on the consistency of objectives. They can also facilitate the attainment of a pattern of policy mixes between each country which are mutually compatible and consistent with the overall aims of growth and stability through providing a background for the necessary decisions on which instruments are to be used, when, and by whom, as well as on the relative weight to be given to the various instruments.

Progress in this area is being made at both an international and Community level. At the Venice summit it was agreed that each of the G-7 countries should develop medium term objectives and projections that are mutually consistent; and that performance indicators should be used to verify that there are no significant deviations from the intended policy course. Within the Community, an indicator-based process is under consideration. The Monetary Committee has recently had a discussion on the basis of a paper submitted by the Commission. The indicators developed within the EMS need not be the same as those developed at the international level although both sets should of course be consistent and complementary.

The Community's battery of indicators should take into account the special circumstances of the EMS. As well as considering the sustainability of current account positions, they must give weight to the objective of exchange rate stability. Also they must be geared to the need to establish as far as possible a common view of the position of the EMS vis-à-vis the exterior. This does not yet imply defining a target zone or reference range for the ECU vis-à-vis the dollar and yen, which would not be realistic or significant in the absence of an agreement with the monetary authorities competent for those two currencies. But as external shocks have the capacity to cause tensions both directly and indirectly, the System cannot be indifferent to them. The Community's procedure should also take into account any decisions made in the context of G-7 surveillance, and should check their consistency with EMS requirements.

The potential effects of the Community surveillance procedures are dampened by the lack of full participation of all currences within the exchange rate mechanism of the EMS. Any mutual consistency exercice is clearly affected by the degree of commitment to the existing pattern of exchange rates.

III.2 Shorter-term Monitoring

Increased capital mobility and the further integration of financial markets will enhance the need for an effective early-warning system to detect disturbances and tensions in the System. As the distinctions between domestic and external markets are reduced, shocks of both a policy and a non-policy nature have more and more direct repercussions between Member States, making it necessary to take a joint view of developments and to establish as far as possible a common line of action.

Given the exchange rate constraints of the System, this joint view should concentrate on the following areas:-

- the fluctuation of exchange rates within the bands, as a more co-operative approach to the use of these margins could both discourage speculation and could help prevent realignments;

- interest rate differentials, which should play a key role in maintaining the stability of the parity grid in the short-term;

- intramarginal interventions, which can at times be a useful additional instrument together with interest and exchange rate policy.

The internal management of the System can only take place against a background of an agreed appreciation of the external situation, which will also have to concentrate on: the exchange rate of the ECU vis-à-vis the major international currencies, interest rate differentials, and the appropriateness of intervention.

Given their respective competences and the differences in Member States over the body which bears the primary responsibility for the various decisions that have to be made and implemented, it is normal that both the Monetary Committee and the Committee of Central Bank Governors should regularly devote attention to these topics.

III.3 Mechanisms and Institutions

The System's mechanisms are continuously evolving in response to changing internal circumstances, and to developments in the world economy. At times modifications of texts as well as practices is also necessary. It is also appropriate to ask whether there should not be some evolution in the institutional arrangements. At this stage these considerations concern: the practice of intervention and its financing; the ECU; and the European Monetary Co-operation Fund.

a) Intervention

As increased capital mobility will increase the potential for destablising capital flows triggered by financial rather than by fundamental shocks, larger interventions may at times be necessary. It should be emphasised that this does not at all mean that the occasions on which intervention is an efficient or desireable policy instrument will increase; if anything, the contrary may be the case because increased co-operation will ensure a better coherence of fundamentals. The necessary magnitudes, when intervention is called for, may however be larger. Also in a strengthened system, based on a higher level of co-ordination, there is an increased justification for some common financing.

At the fluctuation limits intervention is automatic, potentially unlimited, and the financing arrangements are predetermined using the Very Short Term Financing Facility (VSTF). Some strengthening of the VSTF is however appropriate. As experience has shown that capital reflows can take some time, the duration of the credit should be extended and the ceiling increased for the amount which can be automatically renewed.

Intramarginal interventions also have a role to play within the System. The total size of interventions will in many cases be smaller if intervention is undertaken early rather than if currencies are allowed to reach their bilateral limits. The weaker currency loses less reserves, and the stronger has to support a smaller potential disruption to its domestic money market. Intramarginal intervention can also spread the monetary consequences of intervention if it is undertaken in ECU rather than an individual currency. As the gains are flowing to the whole system, there seems to be little reason why the procedures should not be better co-ordinated. Also the resulting interventions could, at least in some cases, be financed by Community mechanisms, especially in cases where the decisions had been made in the context of the joint monitoring of the shorter term tensions in the System, which could have taken into account the divergence indicator.

b) The ECU

The System loses an element of symmetry because the ECU is not at its centre as was initially envisaged. The official ECU is at the moment subject to an acceptability limit of 50 percent. This should be raised to 100 percent. Also its use is limited by the mechanism used for its creation. This mechanism could be improved both by increasing the duration of the swap periods - i.e increasing it from 3 months to for example a year - and by making the swap system permanent.

The status of the private ECU can also be improved. Links between the private and the official ECU should be tightened. It should be possible to use the mobilisation mechanism to obtain private ECU as well as dollars or Community currencies. Especially if it was agreed in the context of the regular monitoring procedure that intramarginal intervention in ECU would be in the interests of the System, there should not be this discrimination against the ECU.

As with the use of any monetary instrument, the decision to intervene in ECU should be based on an overall view, but an improved divergence indicator could provide a useful additional element in the decision-making process. This indicator, which was intended to add a further element of symmetry to the system, has not been used mainly because of the extent of unilateral unco-ordinated intervention, which biases its signals. If intramarginal intervention was to become more co-operative and co-ordinated, the technical problems with the indicator could be rectified and its threshold lowered.

c) The EMCF

Although it could be possible to obtain private ECU for intervention through the mobilisation of official ECU, it would be more simple to create them through a deposit of Community currencies with the EMCF, as was envisaged in the Annex to the Conclusions of the European Council held in Bremen in July 1978. It was there suggested that member state currencies would be transferred in an amount of a comparable order of magnitude to the transfers of gold and dollars. The ECU created against Community currences could be made indistinguishable from private ECU, and could be used for intervention. They would not impede in any way on the existing official ECU circuit.

Under present conditions, interventions in private ECU only have small monetary effects in the countries of the basket currencies; i.e their monetary consequences do not differ very much from intramarginal interventions in EMS currencies. If ECU created through the EMCF were used for intervention purposes, there would be wider monetary consequences. This however is already the case when national central banks are involved on both sides of the transaction as in the case of intervention at the margins. The difference with an ECU intervention would be that it would spread the monetary consequences more broadly.

It should also be asked whether the shorter-term monitoring process, which should be at the base of a better co-ordination, should not take place within the framework of the EMCF. Article 2 of the Regulation establishing the Fund states that it shall promote the proper functioning of the margins of fluctuation of the Community currencies against each other, and interventions in them on the exchange markets.

COMMISSION
OF THE
EUROPEAN COMMUNITIES

The President

Brussels, 30 July, 1987.

CONFIDENTIAL

Special measures in favour of highly indebted low-income countries in sub-Saharan Africa

I. BACKGROUND

1. In preparation for the Venice Summit and at the request of the Member States, the Commission sent COREPER an informal communication[1] on a Community initiative for certain highly indebted low-income countries in sub-Saharan Africa, stressing:

   (i) the exceptional seriousness of the situation of a number of low-income countries in sub-Saharan Africa which have large public-sector debts, particularly with multilateral bodies;

   (ii) the danger that this situation might lead the authorities of the countries concerned seriously to consider abandoning the highly promising reform and austerity policies which they have courageously adopted over the last few years and which are now needed more than ever;

   (iii) the urgent need for exceptional measures to reduce the burden of debt service and restore imports to levels which are more in line with essential consumption and growth requirements;

   (iv) the appropriateness of an initiative by the Community and its Member States, justified not only by the facts of the situation but also by their particular responsibilities towards this part of the world, where they account for more than half of total aid from OECD countries.

2. In this spirit the Commission suggested that:

   (i) the Member States declare themselves ready, within the framework of an overall approach in conjunction with their OECD partners, to take a range of measures including: softening the terms of Paris Club rescheduling, continuing the retroactive adjustment of aid terms and providing further concessional funds, both bilateral and

[1] SEC(87) 904, 3 June 1987.

multilateral (e.g. the proposal for an increase in the resources of the IMF Structural Adjustment Facility);

(ii) the Community as such help these countries by:

- setting up a 100 million ECU special programme to provide quick-disbursing aid financed partly by recycling existing and future funds from the repayment of special loans and risk capital previously granted to ACP States;

- speeding up the commitment and disbursement of the financial resources available under Lomé III by increasing the proportion of quick-disbursing operations, particularly in the form of sectoral import programmes.

3. In giving its broad approval to the Commission's analysis and the general framework for future concerted action to deal with this situation, COREPER indicated its agreement that Community representatives should tell the Venice Summit that all Member States were ready to take appropriate measures, provided OECD partners were prepared to take similar measures.

COREPER also noted the Commission's intention of sending a formal communication in the light of the Venice Summit results spelling out how the specific Community measures would be implemented.

4. Thanks to the catalytic effect of speeches by representatives of Member States and the Community, debt problems received particularly close attention at the Summit. It was recognized that the problems of the highly indebted low-income countries - in particular those in sub-Saharan Africa - needed to be treated as a special case, and that a position shoud be agreed before the end of the year on the various proposals put forward.

This analysis and approach were most recently confirmed during a meeting organized jointly by the IMF and the IBRD (Paris, 10 July) to which members of the Group of Ten, Switzerland and the Commission were invited.

5. In order to consolidate this achievement and apply it in practice, the efforts undertaken before the Summit must be actively continued, both in the form of concerted action by the Member States and action by the Community itself, so that decisions are reached and concrete actions undertaken in the time-scale specified in the communiqué.

II. CONCERTED ACTION BY MEMBER STATES

6. In this spirit, Member States must:

(i) confirm that they are ready, in conjunction with other creditors and donors, to take special measures in favour of the countries concerned, to be selected from the range of measures referred to at 2(i) above;

(ii) cooperate closely within the relevant Community bodies so that they can play an active, coordinated part in forthcoming international discussions (Paris Club; meetings of IMF/IBRD statutory bodies);

7. In this context particular attention should be paid to:

(i) increasing the Structural Adjustment Facility: the meeting on 10 July showed that the bulk of the work of translating the new impetus given by the Summit into practical terms remained to be done, both as regards the size of the proposed increase and the means of financing it;

(ii) the terms for Paris Club debt rescheduling: a consensus seems to have been reached on the need to lengthen grace and consolidation periods. This was confirmed by the very recent decision on the rescheduling of Somalia's debt (which follows earlier decisions concerning Zaire, Mauritania and Mozambique).

However the proposal to reduce interest rates on rescheduled debts remains completely open, if not blocked. It would be useful to hold consultations on this point at Community level in advance of the forthcoming discussions within the Paris Club;

(iii) continuing the retroactive adjustment of ODA terms: Canada has just announced the completion of the exercise cancelling its ODA claims on sub-Saharan Africa. It would be useful to know exactly how much room for manoeuvre there is still in the Member States;

(iv) increasing quick-disbursing aid: more detailed knowledge of Member States' intentions would be useful.

III ACTION AT COMMUNITY LEVEL

8. Special programme: the Commission has just sent the Council a formal communication concerning implementation by the Community in 1988 and 1989

of a special 100 million ECU programme in the form of quick-disbursing aid, in addition to funds provided under Lomé III. Part of the funding for this programme (40 million ECU) would come from the outstanding balances from earlier Conventions and the rest (60 million ECU) from the partial recycling of current and future funds from the repayment of special loans and risk capital granted earlier to ACP countries.

Examination of the proposals contained in this communication must be given priority in the capitals and relevant Community bodies so that a decision can be taken as soon as possible, and in any case before the end of the year.

9. Speeding up Lomé III payments: the Commission confirms its intention of increasing the proportion of quick-disbursing aid for these countries to about 20% of national programmable aid, without changing the priorities and guidelines agreed during the programming exercise. This figure is an overall objective, which would vary from country to country depending on the wishes and needs of the recipients.

Papers P50

From: Sir G.Littler
Date: 25 August 1987

MR PERETZ (o.r.)

c.c. **Mr Alex Allen**
Sir P.Middleton
Mr Scholar
Mr Huw Evans
Mr Mountfield
Mr Kelly
Mr Ilett
Mr Walsh
Ms Life
Mr Loehnis (B/E)

INFORMAL ECOFIN: COMMISSION PAPERS

The Commission have circulated for the informal ECOFIN meeting on 12 September in Denmark a long paper on "Complete Liberalisation of Capital Movements and Strengthening of the EMS", and a shorter paper on Sub-Saharan Africa. The second paper could be helpful to our attempts to promote agreement on the Chancellor's proposals on Sub-Saharan debt and should be covered in briefing to this end. In this minute I am concerned with the first paper.

2. As you know there will be other material available for the meeting on this subject, including a Monetary Committee Report yet to be written. On some past occasions on much the same subject we have had Commission papers which have attracted little attention in the discussion. Not all Ministers have read the documents in advance. Comments have been made haphazardly (in keeping with the informal nature of the discussion). The Chairman has given a (frequently idiosyncratic) summary. The Commission have been left to take note or not as they wished.

3. On this occasion I shall recommend the Chancellor to take this particular paper rather more seriously. It sets out quite a range of ideas about progress towards the future internal market

in which we have a strong interest, and some of them are not at all what we would wish to see. The meeting will be much the best opportunity for getting some UK views on the record, I hope with support, which all of us can then press the Commission to take into account as they develop their ideas.

4. We should aim for a short speaking-note specifically aimed at the Commission paper. After some words welcoming the thrust, careful thought, etc, we want some crisp comments addressed to any significant points of worry. Ones which strike me are listed below, but please would you and others, especially Mr Scholar and Mr Ilett and Mr Loehnis, see whether you agree or have other ideas to offer.

5. My list is:

- Section I: The last paragraph foreshadows prolongation of the 1972 Directive on a basis which could well require members to retain an exchange control capability: we must speak against this.
- Section II.1: I think the 'anti-laxity' theme attacks Italy, Greece, etc rather than the UK; but is there any comment made which worries us? Let us not appear to endorse the 'White Paper' by default, if there are any unacceptable propositions in it.
- Section II.2: On the fiscal front we need to think about both the evasion problem (the Danish Presidency are keen on this because they apparently rely on reporting by banks, etc, to disclose taxable incomes), and about any harmonisation of tax systems, e.g. treatment of dividend and interest incomes, which may be advocated.

- Section III.1: No need to rise to the passing allusion to the absence of sterling from the ERM! The indicators stuff is pretentious but need not be discussed in this context.
- Section III.3: I suggest leaving VSTF and intra-marginal intervention until my bilateral with Trichet, but could you and the Bank please advise on the ECU and EMCF ideas (which I regard with scepticism and which I guess will be hotly opposed by the Bundesbank).

GL

(Geoffrey Littler)

Jonathan ~~ PS? ~~ ALEX O/R

FROM: JANET BARBER
DATE: 25 AUGUST 1987

MR MOUNTFIELD
MR BONNEY
MR BATT
MR BOARD
MR SAVAGE
MS FRENCH C&E
MR COOKE D.TP

cc PS/Chancellor 12/2
Sir Geoffrey Littler
Mr Lavelle
Mr Edwards
Mr H Evans
Mr Peretz
Mrs Lomax
Mr Mortimer
Mr Walsh
Mr Matthews
Mr Kelly
Ms Sinclair
Mr Crabbie
Mr Osborne
Mr Donnelly
Mr C Evans
Mr May
Mr Williams
Miss Wright
Mr Bostock - UKREP
Mr Erskine - B of E
Mr Wood - ODA

INFORMAL ECOFIN 11-13 SEPTEMBER: BRIEFING

The agenda for the informal ECOFIN, which the Chancellor will attend, is likely to be as follows:

1. Strengthening the EMS and liberalisation of capital movements

2. Preparation for the IMF/IBRD annual meetings, especially:

   (a) approval of the EC presidency speech;
   (b) international economic situation;
   (c) international debt and the proposed increase in the resources of the Monetary Fund's Structural Adjustment Facility;
   (d) G10 business.

3. The economic outlook in the Community.

4. Tax approximation.

5. 1988 Community budget and reference framework.

6. Economic situation in Greece.

BRIEFING

<u>Strengthening the EMS and liberalisation of capital movements</u>

2. There will be reports from the Monetary Committee and the Committee of Central Bank Governors. There is also a Commission

paper which has now been circulated by the Danish presidency. Sir Geoffrey Littler, in conjunction with Mr Peretz, will be providing briefing separately on this. (I will try to get a draft of the Bank Governors report from the Bank of England.)

Preparation for the IMF/IBRD annual meetings
3. I understand that the main item under this heading will be sub Saharan debt (on which the Danish presidency has circulated a Commission paper) and the proposed increase in the SAF facility, and that **Mr Mountfield** (in conjunction with IF1) is putting together a special brief for the informal ECOFIN covering these issues.

4. On the economic situation, the Chancellor will be able to draw on the material for the continuation of the July ECOFIN discussion (see paragraph 5 below). I would be grateful if **Mr Batt** could let me know if we need any material on the presidency speech (usually the final Monetary Committee agreed text is acceptable to us). On G10, Sir Geoffrey Littler will brief the Chancellor separately.

The economic outlook in the Community
5. This was discussed at the July ECOFIN on the basis of the Commission's second quarterly review paper. The Danish presidency concluded that the economic situation in the Community should be carefully monitored and reconsidered at this informal ECOFIN (see UKREP telno 2455 of 13 July). I would be grateful if **Mr Savage** could provide a brief on the Commission's paper taking account of recent developments, together with the usual set of economic statistics on the EC, US and Japan.

Tax approximation
6. The possibility of a discussion of tax approximation at this ECOFIN was mentioned by the Germans at the informal ECOFIN in April. The Danes were not particularly keen, and talked about a general debate on principles ranging wider than indirect tax (eg social security) rather than a discussion of concrete proposals. The Danes did not mention tax approximation in the agenda note they circulated at the July ECOFIN, but given German enthusiasm (see UKREP telno 2458 of 13 July), and the fact that this is the first ECOFIN since the Commission produced its proposals, there may be some discussion. I would be grateful therefore if **Ms French** could provide a brief.

The 1988 Community budget and reference framework
7. According to UKREP telno 2458 of 13 July, the Commission, at the July ECOFIN lunch, asked how the Budget Council could set a budget for 1988 constrained by the Council's unrealistic reference framework for agricultural market support. It was agreed that the informal ECOFIN might discuss this matter further. I would be grateful if **Mr Bonney** could arrange for briefing on this.

Economic situation in Greece
8. Following discussion of the economic situation in Greece at its meeting on 15 July, the Monetary Committee chairman will write to the Greek Finance Minister, and report orally to ECOFIN at lunch. There was no indication that there would be much substantive discussion, but I would be grateful if **Mr Savage** could provide a short brief.

BILATERAL DISCUSSION

9. Informal Councils provide a good opportunity for the Chancellor to have marginal discussions with other finance ministers. Perhaps copy recipients would consider whether there is anything they wish the Chancellor to raise with his colleagues, or anything that might be raised with him, and provide briefing accordingly.

10. **Mr Board** has suggested that the Chancellor might raise banking supervision with Stoltenberg, and I would be grateful if he could provide briefing as necessary.

11. I would be grateful if **Mr Cooke** could provide a short brief on the proposed Belgian toll on foreign cars, if there is any chance of anyone raising this with the Chancellor.

FORMAT AND TIMING

12. Briefs should follow the standard format (attached). The aim is to submit the briefing by close on Wednesday 9 September, so individual briefs should as far as possible reach me by close on Monday 7 September.

13. Many thanks for your help

Janet Barber

JANET BARBER
EC1
HM TREASURY

Tel 270-4441

ECOFIN BRIEFING: STRUCTURE OF BRIEFS

General note: be as brief as possible, and try to get objectives and line to take/point to make on first page.

UK OBJECTIVES

These should be stated in a short paragraph. It should be made clear whether the Minister is required to intervene, or whether he will just be participating in a general discussion.

POINTS TO MAKE/LINE TO TAKE

(i) Line to take is appropriate when a proposal is being discussed, and when the Minister is asked to intervene.

(ii) Points to make are for discussion documents where no operational decisions will be reached.

(iii) Line to take/points to make should not include editorial comment except where absolutely essential and square bracketed; they should be set out in skeleton speaking note form, so that the Minister can read from them without further editing.

(iv) Points to make should be interesting i.e not only simple restatements of UK policy where that is well known. It should be remembered that a Minister is limited in the number of points he can make e.g three.

(v) Short Q/A defensive material should be included only if necessary e.g where the Minister will have to argue out a particular point.

BACKGROUND NOTE

Where possible, this should be confined to two sides.

BRIEF

ECOFIN, MARCH 12

SUBJECT

Relevant document:

UK objectives
[If any]

Line to take/Points to make

Defensive briefing
[if necessary]

Background.

ps2/1R

UNCLASSIFIED

pup

FROM: CATHY RYDING
DATE: 25 August 1987

BF to Alex 3/9

SIR G LITTLER

Now you are back from leave, I wonder if you could advise me where we stand on a couple of outstanding issues:

(i) on the informal ECOFIN meetings in September, Alex Allan has asked me to enquire whether you have managed to fix a time ~~for the Chancellor~~ to see Trichet; and

(ii) the Chancellor would be grateful to know the state of play on the Littler/Lebegue Task Force on Sub-Saharan Debt and other matters, post the Balladur meeting.

CATHY RYDING

Alex. O/R.
See minutes below. Geoff has passed on a couple of points on all of this.
On the informal ECOFIN, one possibility is that Balladur & Stoltenburg will go out early for talks. There was some talk (from Stoltenburg I think Geoff said) that the Chancellor should join them. Geoff will sort this out with his opposite numbers. All rather unclear at this stage.

On the Littler/Lebegue Task Force, the first point is that it is no longer Lebegue - but Trichet. — Lebegue has gone to the Central Bank, I think
Geoff will see him on 2 Sept & sort out administrative arrangements for the next meeting of the Task Force. The plan is to meet on 7/8 Sept. Geoff will report to the Chancellor early on the morning of 10 Sept (or by phone if necessary) before the Chancellor leaves for ECOFIN.

CR

CR 26/8

FROM: JANET BARBER
DATE: 1 SEPTEMBER 1987

CHANCELLOR

cc Paymaster General
Economic Secretary
Sir P Middleton
Sir G Littler
Mr Lavelle
Mr Edwards
Mrs Lomax
Mr Mortimer
Mr Ilett
Miss Noble

Mr Bostock - UKREP

C/content with recommendation

CL 1/9

OK, nc Consent. N.

EC INTERNAL MARKET: PROPOSED TRANSFER OF INSURANCE FROM ECOFIN TO INTERNAL MARKET COUNCIL

We have heard from UKREP and other sources that, during their presidency of the Community, the Danes are likely to want to pursue discussion of insurance matters (and possibly some other financial services) in the Internal Market Council (IMC) rather than in ECOFIN, reflecting their own departmental responsibilities. An informal Internal Market Council is being held in Denmark on 7 September, and the proposed transfer may be discussed or announced. Mr Clark will attend this Council, and we understand that he is in favour of a transfer. We need therefore to decide whether we should ask DTI officials to brief Mr Clark to object or acquiesce. This submission seeks your views.

INSURANCE TOPICS DUE FOR COUNCIL DISCUSSION

2. The major insurance item on the table at the moment is the proposed **non-life services directive.** This would lay down rules for the writing of direct non-life insurance across frontiers by insurers not established in the country of the risk being insured. Adoption of a liberal directive has been a UK priority for some time. The last substantive ECOFIN discussion was in December 1984, but then discussion was held up pending the outcome of several relevant European Court of Justice cases. Judgements on these were given in December 1986, but, on grounds of policy holder protection, were not as liberal as we (and the Commission) had hoped. Since then discussion has resumed at working group level, and the Danes hope to obtain Council agreement on a text during their presidency.

3. In addition there are the following insurance items in the current internal market rolling programme:

(a) insurance contract law;
(b) annual accounts of insurance undertakings;
(c) winding up of insurance undertakings.

However DTI do not expect any Council discussion on these during the next year. There may also be discussions in the near future on the EEC-Switzerland insurance agreement, but, again, DTI think that the Council may not need to get involved.

TRANSFER OF INSURANCE TO INTERNAL MARKET COUNCIL

4. You will recall that just before the UK presidency in the second half of 1986, DTI officials asked if they could sound out other member states about taking insurance in the IMC instead of in ECOFIN. When consulted (Mr Mortimer's submissions of 2 and 14 May 1986) you felt then that insurance should stay in ECOFIN because:

(a) since in two key member states, France and Germany, insurance is handled by Finance Ministers, a transfer to the IMC might have impeded progress to liberalisation;
(b) UKREP's advice was that to transfer at the start of the UK presidency might suggest to other member states that you did not attach high priority to progress on insurance.

DTI therefore took the matter no further.

5. This time the position is somewhat different, as we do not hold the presidency. It is also rather confused, as neither the Danes, nor DTI ministers, have made a formal approach to us about transferring insurance (or any other financial services) item to the IMC.

6. On procedure, the presidency does take the lead in deciding Council agendas and allocating Council responsibilities. In principle any member state can ask for a topic to be discussed in any Council if the request is made in time, but exercise of this right in the face of presidency opposition would make Council business unmanageable. In practice therefore the Danes could probably make the transfer unilaterally. Similarly the next presidency (in this case German) could reverse it.

7. On balance, however, we expect the Danes to give some indication of their intention at IMC. Insurance was one of the six key internal market areas identified for early progress at the Brussels European Council, and IMC discussion is to focus on these, and on working methods following the implementation of the Single European Act.

8. On the merits of the transfer, DTI support it mainly because they believe that the UK's aim, the adoption of as liberal a non-life services directive as possible, is more likely to be achieved by co-operating fully with the Danes. The Danes are very much towards the liberal end of the spectrum of member states, and have targetted Council agreement on a text of the directive for their presidency. Although DTI think that agreement this quickly is unlikely, antagonising the Danes in this matter could run counter to UK interests. In addition, DTI feel that their ministers, being responsible for insurance domestically, are better placed to pursue UK priorities in the Council.

9. In the past we have argued that a transfer from ECOFIN to the IMC might impede progress to liberalisation on insurance, since in about half the member states, including France and Germany, insurance is handled by finance ministers, who might be reluctant to give their industry ministers the necessary flexibility. The

DTI argue now that since last year the Germans have become more liberal, and that Italy, where insurance is handled by the industry ministry, has become a more crucial obstacle to liberalisation. France has been making enthusiastice noises about the internal market generally, but it is not clear yet whether they have become more liberal on insurance. Informal contacts with the Germans via UKREP suggests that their finance ministry will not be in favour of transferring Council discussion of insurance to the IMC. (Consultation with the French permanent representation has not been possible because of holidays).

10. A major Treasury concern is that keeping insurance, and other financial services items, in ECOFIN allows the Treasury (and finance ministries in other member states) to keep a central watch on developments, and exercise some control without getting too involved in the detailed work. Allied to this is the worry about DTI ambitions on financial services generally, both in Europe and domestically, and the possibility of pressure to transfer other financial services items, perhaps even those on which in the UK the Treasury leads, to internal market ministers. Therefore FIM feel that although taken in isolation there might be something to be gained by transferring non-life insurance to the IMC during the Danish presidency, they would prefer most other items, including life insurance, to remain in ECOFIN, and believe that a concession on non-life insurance might threaten this.

11. UKREP are neutral about which Council should handle insurance, but would tend to agree with DTI that UK aims on insurance would be best served by co-operating with the Danish presidency. The FCO and Cabinet Office are fairly neutral about the issue.

OTHER FINANCIAL SERVICES

12. Here we have even less idea of what the Danes may be considering. The financial services items currently in the internal market rolling programme, some of which could be expected to come to ministers during their presidency, include the following:

DTI items

(a) UCITS (undertakings for collective investment in transferable securities - ie unit trust type devices) - directives on jurisdiction and investment policy
(b) directive on prospectuses for securities offered to the public for the first time
(c) annual accounts of foreign branches of credit institutions

Treasury items

(d) harmonisation of the concept of banks own funds
(e) re-organisation and winding up of credit institutions
(f) directive on mortgage credit

As indicated above, FIM would prefer to keep all of these in ECOFIN's purview. On the other hand, we understand that DTI ministers do want to be involved in Council discussion of financial services generally, whether in ECOFIN or the IMC.

13. Apart from the strategic argument set out in paragraph 10 above, FIM/Bank of England views on the individual items are as

follows:

(1) we should oppose any transfer to the IMC for **banking** and **mortage credit.** This is predominantly finance ministry business in the Community, and in the UK has little relevance to DTI. If banks own funds was transferred to the IMC, banking supervision and solvency ratios would probably follow. We could however contemplate a transfer on **re-organisation and winding up of credit institutions** (on which we hope no progress will be made anyway), because of its relationship to insolvency policy (for which DTI are responsible).

(2) there is a good case for the **annual accounts of foreign branches of credit institutions** following the bank accounts Directive into ECOFIN. On the other hand, this could equally well be kept with the expected 11th branch accounts directive, which might well go the IMC.

OPTIONS

14. On **insurance**, the prospect of progress on the non-life services directive must be set against the strategic argument set out in paragraph 10. The practical options are as follows:

(a) **oppose** a transfer to the IMC (in the face of the presidency's de facto power). However, we could not necessarily rely on Mr Clark to do this at the informal IMC, and would probably have to make our views known through other channels eg through UKREP or at the informal ECOFIN on 11-13 September. If we took this line, DTI ministers would probably want to write to you about it.

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RECOMMENDATION

16. Given DTI's conviction that UK interests on non-life insurance will be best served by acquiescing in the Danes plan to transfer

discussion from ECOFIN to the IMC, and taking into account the presidency's role in allocating Council responsibilities, we suggest that DTI should be asked to brief Mr Clark along the lines of option (b) above.

17. This submission has been agreed with FIM division.

Janet Barber

JANET BARBER
EC1

ANNEX J1

J1

FROM: JANET BARBER
DATE: 1 SEPTEMBER 1987

CHANCELLOR

cc Paymaster General
Economic Secretary
Sir P Middleton
Sir G Littler
Mr Lavelle
Mr Edwards
Mrs Lomax
Mr Mortimer
Mr Ilett
Miss Noble

Mr Bostock - UKREP

EC INTERNAL MARKET: PROPOSED TRANSFER OF INSURANCE FROM ECOFIN TO INTERNAL MARKET COUNCIL

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<u>Treasury items</u>

(d) harmonisation of the concept of banks own funds

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RECOMMENDATION

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discussion from ECOFIN to the IMC, and taking into account the presidency's role in allocating Council responsibilities, we suggest that DTI should be asked to brief Mr Clark along the lines of option (b) above.

17. This submission has been agreed with FIM division.

Janet Barber

JANET BARBER
EC1

ps2/14R

UNCLASSIFIED

ANNEX J2

J2

FROM: CATHY RYDING
DATE: 2 September 1987

MISS J BARBER

cc Paymaster General
Economic Secretary
Sir P Middleton
Sir G Littler
Mr Lavelle
Mr Edwards
Mrs Lomax
Mr Mortimer
Mr Ilett
Miss Noble
Mr Bostock - UKREP

EC INTERNATIONAL MARKET: PROPOSED TRANSFER OF INSURANCE FROM ECOFIN TO INTERNAL MARKET COUNCIL

The Chancellor was grateful for your minute of 1 September.

2. The Chancellor is content with your recommendation, but with the caveat that all other Member States should be happy.

CR

CATHY RYDING

K

E[C]FIN: 11-13 SEPTEMBER 1987 ANNEX K

BELGIAN PROPOSAL TO TAX FOREIGN VEHICLES USING BELGIAN ROADS (DEFENSIVE)

K

UK Objectives

The Germans or Dutch may criticise the Belgian proposal to introduce a tax on all foreign vehicles using Belgian motorways. The UK should lend low-key support to any such criticisms, but should not associate itself with any threats to retaliate.

Line to take (Only if raised.)

- Hope Belgians will drop this idea. Such a tax would create an obstacle to free movement and run counter to completion of the internal market.
- Difficult to see how this tax could be applied in a way which did not discriminate against foreign vehicles contrary to the EEC Treaty.
- Also unhelpful in EEC dealings with Switzerland (who have such a scheme of their own which we should like to see removed) and Austria (who are working on similar proposals).

Background

Belgian Government are considering requiring foreign vehicles to purchase a tax disc (vignette) to pay for their use of Belgian motorways. The disc would be valid for a year and the proposed charge is reported to be 750 Francs (£12.45) for cars and 1,500 Francs (£24.90) for lorries. This is a revenue-raising measure rather than a transport measure.

Dutch and German Transport Ministers have already made strong protests to Belgian Government and Minister of State in DTp (Mr David Mitchell) has also written to the Belgian Transport MInister to express concern. The Germans have asked for the matter to be put on the agenda of a Transport Council. There are some indications that these protests are causing the Belgians to think again.

Tolls on certain UK bridges and tunnels are not comparable with the general tax which the Belgians have in mind, as they apply to all vehicles using those specific crossings.

PERSONALITY NOTES

20/12

COVERING CONFIDENTIAL

PERSONALITY NOTES

Belgium

1.	Mr Philippe Maystadt	Minister for Economic Affairs
2.	Mr Mark Eyskens	Minister for Finance

Denmark

3.	Mr Anders Andersen	Minister for Economic Affairs
4.	Mr Palle Simonsen	Minister for Finance

France

5.	Mr Edouard Balladur	Minister for the Economy, Finance

Germany

6.	Dr Gerhard Stoltenberg	Minister for Finance
7.	Dr Martin Bangemann	Minister of the Economy
8.	Dr Otto Schlecht	State Secretary - Federal Ministry of the Economy
9.	Dr Hans Tietmeyer	State Secretary - Federal Ministry of Finance

Greece

10.	Mr Dimitris Tsovolas	Minister for Finance

11.	Mr C Simitis	Minister of National Economy
12.	Mr Athanasopoulos	Alternate Minister of Finance

Ireland

13.	Mr R MacSharry	Minister for Finance
14.	Maurice F Doyle	Secretary - Department of Finance

Italy

15.	Mr Giuliano Amato	Minister for the Treasury

Luxembourg

16.	Mr Jacques Santer	Prime Minister and Minister of Finance
17.	Mr Jean Claude Juncker	Minister of Labour, Minister Delegate for Finance, responsible for the Budget
18.	Mr Jacques Poos	Vice-President of the Government Minister of the Economy
19.	Mr Pierre Werner	Honorary Minister of State

Netherlands

20.	Dr Ruding	Minister for Finance

Portugal

21.	Dr Miguel Jose Ribeiro Cadilhe	Minister of Finance

Spain

22.	Mr Carlos Solchaga Catalan	Minister of the Economy and Finance

Secretariat

23.	Mr Ersbøll	Secretary General of the Council Secretariat

Commission of the European Communities

24.	Mr Jacques Delors	President
25.	Lord Cockfield	Vice President (not attending)
26.	Mr Christophersen	Vice President
27.	Mr Andriessen	Vice President
28.	Mr Willy De Clercq	Member

MAYSTADT, PHILIPPE

Economic Affairs

Minister for ~~the Budget, Scientific Policy and Planning~~. Former Minister for the Civil Service and Scientific Policy (1980-81). Deputy for Charleroi since 1977.

Born 1948. Spent 2 years in the US where he gained a degree in Public Administration at the University of Los Angeles. He also has a law degree from Louvain University. State Secretary for the Walloon region (October 1979-April 1980).

A young and articulate politician with an important portfolio, who has an enthusiastic following among the younger members of the PSC. One of the few members of his party to improve his standing in the November 1981 elections and a possible future leader.

Married with three young children. Speaks quite good English.

EYSKENS, MARK

Minister for Finance ~~Economic Affairs~~. Former Prime Minister (April-December 1981) and Minister of Finance (October 1980-April 1981). CVP Deputy for Leuven since April 1977.

Born Leuven 1933.

Son of former Prime Minister, Gaston Eyskens. Doctorate from Leuven University (KUL) and MA from Columbia University. Adviser to Finance Minister 1962-65, Professor of Economics at KUL since 1966. Commissaire-Générale responsible for links between the French and Dutch speaking universities of Leuven (UCL-KUL) since 1972.

Held office in both Tindemans' governments, first as State Secretary for Land Management and then as State Secretary for the Budget and Flemish Regional Economy. Served as Minister for Cooperation and Development under Martens, April 1979-October 1980.

An eminent economist and influential adviser to his party on economic matters, on which he generally takes a conservative line. As State Secretary for the Flemish Regional Economy he was active in seeking new investments for Flanders, especially from the United States, whose diminished confidence in Belgian economic prospects he tried hard to revive. He brought a change of style to the Cooperation and Development Ministry where he attempted to alter the pattern of Belgian aid, hitherto directed almost exclusively to francophone countries.

He is married. Both he and his charming wife speak excellent English, are very sociable, and are seen about more than any other Belgian Minister.

ANDERSEN, ANDERS

Minister of Ecomomic Affairs (Venstre) since September 1982.

Born 1912. Member of the Folketing since 1953. Chairman of Federation of Jutland Agricultural Societies 1959-73. President of Agricultural Council 1960-73. Co-Chairman of Federation of Danish Agricultural Societies (the 'middle size' farmers' union) 1960-73. Member of the Board of Representatives of National Bank 1970-73 and since 1976. Declined to compete for leadership of Venstre in 1965 and turned down the post of Minister of Agriculture 1968. Minister of Finance 1973-75. Minister of Economic Affairs and Taxation 1978-79.

A dogged parliamentarian and negotiator, he operates very much behind the scenes in the present administration, taking on the tough task of pursuading recalcitrant trade unions and employers' groups to swallow the Government's nastiest medicine. Married. He is polite but unforthcoming in conversation - not very easy to extract information from. Limited English.

4

SIMONSEN, PALLE
MINISTER OF FINANCE SINCE JULY 1984.

Minister for Social Affairs (Conservative) ~~since~~ FROM September 1982. UNTIL JULY 1984

Born 1933. After training at a business school in Jutland, worked in industry. Member of the Folketing 1968-75 and since 1977. Chairman of the Defence Committee for several years. Deputy Chairman of the Conservative Party since 1975. Member of the Radio Council and the Civil Defence Council. Would have preferred Defence portfolio, but was pressed to take what was seen as the more difficult Social post, where he seems to be doing well. Met Mr Norman Fowler briefly in March 1983. Visited Britain as guest of Government to study defence early 1982. Some tip him for high office. Helpful over visit by House of Commons Select Committee on Social Affairs 25-26 April 1983, when they studied Danish policy on children in care.

Married: both speak English. Very approachable and ready to accept invitations. Active in local charities in Gentofte.

BALLADUR, EDOUARD

Minister of the Economy, Finance and Privatisation.

As the only Minister of State in the Government, clearly the most important figure after Chirac. He will supervise Junior Ministers for the Budget, Privatisation and Foreign Trade. Born 1929. ENA. 1963-74 worked for Pompidou, first as Social Affairs Adviser (alongside Chirac) when Pompidou was Prime Minister, later Assistant Secretary-General of the Elysee in 1969 and Secretary-General in 1973. After Pompidou's death in 1974, Head of a Subsidiary of the CGE Electronics Group before moving back into the political world in the late 1970s as an increasingly influential adviser to Chirac.

~~Although largely unknown to the French public (he had not stood for elected office before last Sunday),~~ He is intelli gent, calm and discreet and has a high reputation for efficiency and good sense. He has little direct experience of the Ministry he now directs or of financial affairs and, while open-minded, is generally seen as prudent rather than particularly liberal in his approach to economic affairs. This is in contrast to the more obviously liberal approach of other ministers in the economic field, notably Juppé (Budget), Noir (Foreign Trade) and Madelin (Industry).

STOLTENBERG, DR GERHARD, HON GCMG

Federal Minister of Finance.

Born 1928 in Kiel, the son of a clergyman. War Service 1944-45. Studied history, social science and philosophy at Kiel University, taking his doctorate in 1954 with a thesis on the work of the First Reichstag. Thereafter worked as an assistant at Kiel University. Appointed Lecturer in Modern History in 1960, his special topic being Tirpitz and his naval policy. 1965 and again 1969-70, a Director of Friedrich Krupp, and Head of the company's Economic Policy Department.

He entered politics through the Young CDU, of which he was Federal Chairman from 1955-61. A member of the Schleswig-Holstein Land Parliament from 1954-57, and again since 1971. A member of the Bundestag from 1957-71. 1965-69 Federal Minister for Scientific Research. Elected a Vice-Chairman of the CDU in 1969 and from 1969-71 was Vice-Chairman of the CDU-CSU Parliamentary Party. He resigned from the Bundestag in 1971 to lead the CDU compaign in the Schleswig-Holstein Land elections, as a result of which he became Minister-President. Re-elected in 1979 after a hard and close-fought contest. Returned to Bonn as Finance Minister on the formation of the CDU/CSU/FDP Government in October 1982.

Stoltenberg was the first of the younger generation of CDU politicians from North Germany to reach the top rank. He appeared to be Dr Kohl's main rival within the CDU for the nomination in 1975 as CDU/CSU Chancellor-Candidate. But in the event Kohl's control of the party machinery allowed him to out-manoeuvre Stoltenberg completely, and the latter's candidature never got off the ground. This has reportedly left a legacy of some bitterness between them. His age and abilities should ensure him an important future in the CDU. The CDU's unimpressive showing in Schleswig-Holstein in the 1976 and 1980 Federal elections slightly tarnished his image but in the latter contest his loyal support for Herr Strauss' cause (he stood as Vice-Chancellor candidate) earned him much credit with the Union as a whole, particularly in Bavaria. The obvious choice as Finance Minister in Chancellor Kohl's Cabinet.

Stoltenberg is tall, well-built and good-looking. Reserved, even a little cool, but an effective speaker. He is normally courteous and friendly, but occasionally shows signs of impatience or a touch of arrogance. As Minister for Scientific Research, he favoured European cooperation in the scientific field and showed himself well-disposed to the UK. He often refers to the fact that the Angles came to Britain from his Land. Visited the UK as the guest of HMG in 1974.

Protestant. Married. One daughter and son. His wife is quiet and takes little part in her husband's public life. He speaks good English.

MARTIN BANGEMANN

Born in 1934. A lawyer by profession, he joined the Liberal Free Democrat Party (FDP) in 1963 and rose quickly to become Chairman of the Baden-Wuerttemberg party (the FDP's most important region) in 1974. He was elected to the Bundestag in 1969 and became a Member of the Foreign Affairs Committee.

Genscher (Vice Chancellor and Foreign Minister) made him FDP Secretary-General in September 1974. Bangemann never settled in the job. He stands well to the right in the FDP and was out of tune with the party at a time when it was committed to a coalition with the Social Democratic Party (SDP). He felt strongly that the FDP should keep open the option of future coalition with the Christian Democrats (CDU/CSU). His reluctance to lead his party in to the Baden-Wuerttemberg Regional (land) election in 1976 with a commitment to the SPD caused Genscher to engineer his resignation as Secretary-General. Bangemann was subsequently rejected by the Baden-Wuerttemberg party and resigned as regional Chairman in 1978.

He has spent the last four years as leader of the FDP Parliamentar Group in the European Parliament. As a result he has been out of touch with Federal politics and out of the public eye. He re-emerged with his energetic campaign as the FDP's leading candidate in this year's European election. Although the FDP failed to clear the 5 per cent hurdle necessary for representation at Strasbourg, the blame for this has been laid on Genscher, and Bangemann has managed to emerge relatively unscathed.

Bangemann was an effective member of the European Parliament and leader of the FDP group there. He is a genuinely dedicated European. A strong character and a man brimming with bright ideas. He played a leading role in forming the Federation of European Liberal Parties.

In so far as Bangemann has taken an interest in Economics, his views are Liberal. But in a typical German way he also has a strong social conscience. He is a strong believer in détente.

Bangemann is stout, bespectacled, friendly and a keen traveller. He speaks English and French.

SCHLECHT, DR OTTO

Official State Secretary in the Federal Ministry of the Economy.

Born 1926 in Biberach (Swabia). The son of a butcher. War service; American POW. From 1947–52 studied economics at Freiburg University. Joined the Federal Ministry of the Economy in 1953 and has risen rapidly by sheer ability. A non party figure who has served Ministers of different parties with equal success, impressing each in turn. The right hand man of the Economics Minister, Graf Lambsdorff.

In 1967 Professor Schiller made him Head of the Department dealing with economic policy. Following the General Election in 1972 and the resignation of Dr Mommsen he was promoted to his present position where he is responsible for general domestic economic policy and European Community policy.

Schlecht has consistently held the line against attempts to erode the social market economy from within, and although pragmatic in his private view of the policies of others can be relied upon to voice opposition of what he regards as protectionist trends.

A tall, bulky human man, who retains a strong Swabian accent and simple tastes. His Bonhomie and sometimes coarse humour do not mask his ability. Friendly and well disposed towards Britain, but a firm defender of German interests.

Married, no children. Understands English quite well, although prefers to speak through an interpreter. His wife speaks English quite well. Both are keen, not very good, golfers.

TIETMEYER, DR HANS
State Secretary - Federal Ministry of Finance

Born 1931 in Metelen (Westphalia). Studied economics at Münster, Bonn and Cologne. 1959–62 Secretary of Catholic Church organisation. Joined Federal Ministry of the Economy in 1962. 1970 Head of the department dealing with the European Communities and relations with third countries. 1972 Head of the department dealing with economic and growth policy. 1973 promoted to present position.

A South German, friendly and easy in manner if a bit professorial (he spends quite a bit of the time lecturing to professional bodies on behalf of his Minister). Has SPD sympathies, though not a Party man, and has in the past taken a relatively less restrictionist view than some of his economic colleagues. Has a good academic reputation, is highly articulate, and outspoken on his own subject. His views are widely respected. As Chairman of the EC Economic Policy Committee was deeply involved in the EMS and Concurrent Studies and reportedly played fair.

A good contact with an enquiring and objective mind. Married with two children by a first wife who died in 1978. Catholic. Good English.

TSOVOLAS, DIMITRIS

Minister of Finance. Deputy for Arta

Born 1942 near Arta. Studied law at Salonica University then practiced in Arta until 1977 when he was elected as PASOK Deputy.

As a Deputy he has been active in promoting PASOK's interests and before his ministerial appointment he was a lively parliamentarian. Since his appointment as Under Secretary of Finance in 1981 he has kept a low profile. But his promotion in 1984 to Alternate Minister following the resignation of Pottakis, and then to Minister of Finance in July 1985, suggest that he is well regarded.

Married with a son and a daughter.

CONFIDENTIAL

SIMITIS, PROFESSOR CONSTANTINE (COSTAS) now Minister of National Economy

previously Minister of Agriculture. Not a Deputy.

Born Athens 1936. Studied politics in Athens and law in Germany, where he later pursued an academic career. Spent two years at the LSE in the 1960s. Professor of commercial law at the Panteios Higher School of Political Science since 1977, he also maintained a commercial law practice in Athens. A founding member of "Democratic Defence" in 1967, he left Greece secretly in September 1969 and became a leading member of PAK in Germany. A founder member of PASOK, he was a member of the Central Committee and Executive Bureau and one of the party's leading ideologists until he fell out of favour with Papandreou in 1978. Much to his regret, he was not adopted as a parliamentary candidate in 1981, and his apparently sudden return to favour took many by surprise.

His removal from the Executive Bureau in 1978 apparently reflected concern about a possible challenge to Papandreou's authority. But, in or out of favour, Simitis has never wavered in loyalty to the party and its line. Intelligent with a strong personality but an unassuming manner. One of the most capable of the Government. His inner political convictions are difficult to fathom.

Married. Good English and German. Charming wife Daphne also speaks English.

ATHANASOPOULOS, NIKOS

Alternate Minister of Finance. Deputy for Salonica 'A'.

Born 1923 in Arkadia. Attended Patras Agricultural College and the University of Athens, where he studied law. Worked as Deputy Public Prosecutor at the Court of Appeal.

Elected Deputy in 1977, 1981 and 1985. Appointed to his present post in July 1985.

Married with two sons.

MACSHARRY, RAYMOND TD MEP

Fianna Fail Deputy and Honorary Treasurer.

Born Sligo 1948. Educated Summerhill College, Sligo. Member of Sligo County Council since 1967 and of Northern Western Health board since 1971. Deputy since 1969 for Sligo/Leitrim. Opposition front bench spokesman on the Office of Public Works 1973-75. Member, Committee of Public Accounts 1969-77. He was nominated as a Minister of State at the Department of the Public Service in December 1977, in recognition of his outstanding poll in the general election of June 1977. A loyal supporter of Mr Haughey, he was Minister for Agriculture from 1979-81 where he proved his ability.

A relatively competent Minister of Finance in 1982, he came unstuck when he was found to have bugged a meeting with an anti-Haughey deputy. Resigned from the front-bench. Mr Haughey's most loyal supporter in the leadership contests of 1982 and 1983, he is now regarded as a rising candidate for the succession to Mr Haughey. A hawk on Anglo-Irish relations, but argued for abstention on the Anglo-Irish Agreement, 1985.

Married Elaine Neilan. Three sons, three daughters.

MAURICE F DOYLE

Secretary, Department of Finance

Born in Dublin, 1932. Educated at the O'Connell Christian Brothers School; University College Dublin (BA in Economics), and Kings Inns Dublin (Barrister at Law).

Mr Doyle entered the Irish Civil Service as an Administrative Officer and, apart from two years in the Office of the Revenue Commissioners, has worked exclusively in the Department of Finance. He was involved in the preparation of Dr Whitaker's paper "Economic Development" which laid the foundation for Irish industrialisation and rapid economic growth. For a time he was Assistant Secretary to the National Industrial and Economic Council. He led the official Irish negotiating team on the establishment of the EC Regional Development Fund and was elected the Vice Chairman of the EC Regional Policy Committee. In 1976 he was appointed Second Secretary in charge of economic policy and in 1977 assumed responsibility for control of public expenditure. He was appointed Secretary of the Department on 1 November 1981.

He is an impressive official, frank and friendly. He has not been linked to either political party and has a civil servant's somewhat cynical view of the motives of his political masters.

He is married with two children.

AMATO, ONOREVOLE GIULIANO

Under-Secretary in Prime Minister's Office (Socialist).

Born at Turin in 1938, but lives in Rome. Professor of Constitutional Law at Rome University. Joined the PSI in 1958 and became a member of the Party Central Committee in 1978. Author of a number of books on constitutional questions. President of the Commission for the Review of the Office of the Prime Minister in 1979 and President of the Commission for the Reform of State Holdings in 1980. Has held university teaching posts in the USA.

Elected Deputy for Turin-Novara-Vercelli in June 1983. Diminutive, intelligent and very hard-working: known as "the subtle doctor". His big chance came after the 1983 elections when Craxi took him to Palazzo Chigi to be Secretary to the Council of Ministers (Cabinet). A follower of Giolitti (qv) and bitter critic of Craxi during the 1970's, he has now burnt his boats with the PSI left and become Craxi's right-hand man. In the absence of any formal structure for interministerial coordination, Amato has built up an active rôle for himself as Prime Ministerial "Chief of Staff". Respected for his skills in negotiation and public presentation of policy, he has played a central rôle at times of crisis (such as the Achille Lauro hijacking in 1985), and has general oversight under Craxi of coordination of action against terrorism.

Speaks English well.

16

SANTER, JACQUES

Prime Minister since July 1984

Minister of State, President of the Government, Minister of Finance, of National Development, and of Posts, Telecommunications and Information Technology. Leader of the Christian Social Party.

Born 1937. Education in Luxembourg, Strasbourg and Paris, where he obtained a doctorate in law. 1961-65 Lawyer at the Luxembourg Court of Appeal. 1963-65 worked as a Civil Servant in the Private Office of the (Socialist) Minister of Labour and Social Affairs. Government Attaché to the Ministry 1965. 1966 Secretary to the Christian Social Party's parliamentary group. 1970 Assistant General Secretary of the Party. 1972 State Secretary for Labour, Social Services and Culture. The same year became General Secretary of the Christian Social Party, and its President from 1974-84. Member of the Luxembourg Chamber of Deputies since 1974. Member of the European Parliament from 1974-79, when he was re-elected but appointed Minister of Labour, Social Security and Finance. Elected leader of the Christian Social Party in December 1983 in succession to Pierre Werner.

A strong performer on EC matters, he is now the doyen of EC finance ministers. He is able and friendly. Although in the past he was accused of lack of substance, he has shown himself a competent administrator and is growing in assurance. His public bonhomie conceals a good brain.

Speaks English but prefers French. COI visitor (1973).

Has an attractive and vivacious French wife who teaches biology, but is something of a liability for her husband's political prospects (eg in speaking not a word of Luxembourgish).

Minister of Labour. Minister Delegate for Finance, responsible for the Budget.

He is a lawyer. In 1979 he became Secretary of the Christian-Social parliamentary group and National President of the Christian-Social Youth Organisation. Appointed State Secretary for Labour and Social Security in December 1982 at the age of 28, the youngest ever member of a Luxembourg government.

A capable and forthright young man.

CONFIDENTIAL

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POOS, JACQUES

Vice-President of the Government, Minister of Foreign Affairs, Foreign Trade and Cooperation, of the Economy, of the Middle Classes and of the Treasury. (Socialist).

Born 1937. Educated Lausanne University where he obtained a Doctorate in Economic and Commercial Science. 1959-62 Attaché at Ministry of Economic Affairs; 1962-64 Head of Research at the Government Statistical Service. In 1964 appointed Director of the Socialist daily, 'Tageblatt', though he relinquished day-to-day editorial responsibility when elected to the Chamber of Deputies in 1974. He became Leader of the Parliamentary Group of the POSL in 1975 and in June 1976 was elected to the party's Executive Committee. Minister of Finance 1976, at the same time becoming a director of the World Bank, IMF and the EIB and of the Banque Continentale de Luxembourg and Paribas. Re-elected to the Chamber of Deputies in 1979, and appointed one of two Vice-Presidents of the Socialist Parliamentary Group. Led the POSL in the 1984 elections, gained the highest personal vote of all the candidates, and played a large part in the formation of the coalition with the PCS.

He is a clever, though rather vain man and an ambitious politician. As editor of the 'Tageblatt' he occasionally advocated extreme policies, but he mellowed after entering the Chamber of Deputies and proved an uncontroversial Minister of Finance.

His chief interests at the MFA are economic and financial matters. He leaves political affairs outside the EC largely to his State Secretary, but he has the reputation of always reading and commenting on his briefs and being willing to learn.

Has written several books on economic and financial matters. Married for the second time. His wife devotes herself to her family and seldom accompanies her husband to official functions. 3 children, one of them by the first marriage.

Speaks good English. His wife prefers French.

Honorary Minister of State (Christian Social).

Born near Lille in 1913. Educated in Paris. Doctor of Law (1938), but soon left the Bar for the Banque Generale. 1945 appointed Banking Control Commissioner. 1953 appointed Minister of Finance and (1954) of the Armed Forces. Prime Minister from 1959 of successive coalition governments; with the Democrats (1959-64 and 1969-74); and with the Socialists (1964-69).

A very impressive public servant who has commanded widespread respect and esteem during his long years of office, not least for the patience he showed in allowing decisions to emerge by consensus. An excellent speaker. In the 1974 elections his party lost a number of seats and though it was still the largest party, he decided to resign, devoting a year to the organisation of the party. The considerable success of his Party in the 1979 elections was largely due to his efforts. Following M Thorn's departure from Luxembourg politics at the end of 1980, M Werner's commanding political position increased and there was general regret when he left politics after the 1984 elections. He is extremely well-informed on Luxembourg affairs but since his retirement he seems to have lost some of his interest in politics, and tires more easily.

He is well-known internationally as a speaker and writer, especially on financial matters. Much of the credit for the growth of Luxembourg as a financial centre belongs to him. Paid an official visit to the UK with his wife in October 1982.

M Werner has a relaxed, friendly, open and attractive personality. He inspires confidence with his peasant shrewdness and sophisticated intelligence. From 1979 to 1984 he was Prime Minister and Minister of Culture, Religious Affairs, Information and the Press, Development and the Treasury. He speaks fluent English and listens to the BBC every morning. He understands better than most the British way of doing things. He is a devoted family man, fond also of music (he is a good pianist) and gardening. His wife died in January 1984 after a long illness. 5 children.

DR H O C R RUDING (CDA)

Minister of Finance (since November 1982) for the Netherlands.

Born in Breda in August 1939. Grew up in a Catholic family. Studied at the Rotterdam School of Economics (later Erasmus University). 1965 to 1970 Head of the International Monetary Affairs Division of the Ministry of Finance. 1971 to 1977 Managing Director of the AMRO Bank in Amsterdam. 1977 to 1980 Executive Director of the IMF in Washington. 1980 to 1982 member of the Board of Management of the AMRO Bank.

A friend of the new Prime Minister, Lubbers, from University days. Ruding was first offered the Finance Ministry in 1980 when Andriessen resigned, but on that occasion he turned it down.

CONFIDENTIAL

Dr Miguel Jose Ribeiro Cadilhe

Minister for Finance

Born 10 November 1944 in Barcelos. Graduated in Economics at the University of Porto and did research at the London School of Economics. Has pursued a career teaching and writing about economics before serving as Secretary of State for Planning between 1981 and 1983, and subsequently headed the Department of Economic and Financial Studies of Banco Portugues Do Atlanttico in Oporto. Friendly and intelligent, though his approach can seem more academic than practical. Speaks fair English.

Married (Antonia) with one son.

SOLCHAGA CATALAN, CARLOS

Economy and Finance Minister since 4/7/85

Minister for Industry and Energy since 1982; PSOE Deputy for Alava since 1979.

Born 1944 in Navarre. After reading Economics at Madrid University entered the research department of the Bank of Spain. While in the Bank spent two years at the MIT in Cambridge, Massachussets, doing further research. With the Bank of Spain until 1974, when he joined the Research Department of the State industrial holding, INI, for a brief spell. Began to take an active interest in politics in early 1975, when he joined both the PSOE and the UGT. Head of the Research Department of the Banco de Vizcaya in Bilbao in 1975-77. Joined the Basque Socialist Party in 1978, and elected to the Executive.

An intelligent and fluent speaker, he was one of the leading lights of the PSOE in Congress debates on the economy. He made his name during the debates on the vote of censure motion against Suarez (q.v.) in May 1980. He was influential in drafting the PSOE's economic programme before the 1982 elections.

As Industry Minister he has borne the brunt of criticism arising from the government's programme of industrial restructuring in the steel and shipbuilding sectors. Gonzalez (q.v.) refused his offer to resign in 1983, when criticism reached a peak. Solchaga's talent is unquestioned and in the event of a government reshuffle he would expect another job.

Married with two children. Speaks English and French.

ERSBØLL, NIELS (DANISH)

Secretary-General of the Council since October 1980.

Born 1926. Graduated in Law. Joined MFA 1955, served Paris (Mission to NATO) 1958-60, EFTA Secretariat, Geneva 1960-63 MFA 1964-73. Permanent Representative to EC 1973-77. Second Permanent Secretary for Foreign Economic Affairs in the Ministry of Foreign Affairs 1977-80, responsible for economic and Community affairs. Chairman of the International Energy Agency in Paris 1979-80.

A charming man, who speaks excellent English. Always calm, courteous and intelligent. He had much to do to clear up the staff troubles which his predecessor bequeathed to him.

Married; his wife is an economic journalist.

Confidential

President of the Commission since January 1985.

DELORS, JACQUES

Minister for the Economy and Finance. (Ministre de l'Economie et des Finances).

Born 1925. Worked for the Banque de France and later the Economic and Social Council. Counsellor for Social Affairs in the Commissariat-Général of the Plan, 1962-68. A member of the French equivalent of the Consumers' Association (a Government body) 1968-70. Secretary-General of the Inter-ministerial committee for Industrial Training and Social Affairs 1969-73. Appointed adviser to the Prime Minister on Social and Cultural Affairs, June 1969 and from 1971-72 Chargé de Mission in the Cabinet of M. Chaban-Delmas when he played an important part in the development of Chaban's 'new society' policy. M. Delors is in particular credited with the idea of long term progressive wage contracts (contrats de progrès) in the public sector. He left the Inter-Ministerial Committee in 1973 to take a position at the University of Paris-Dauphine where he lectured on social policy and became an Associate Professor. Founded the 'Association 1973-80' to study economic, social and environmental planning in 1973. Member of the Board of the Bank of France, 1973-79. Joined the PS at the time of the Presidential election in 1974. 1976-81 he was the Party's National Delegate for international economic affairs. Elected an MEP in 1979, he was President of Economic and Monetary Commission of the European Parliament. During the 1981 Presidential election campaign, he acted as one of M. Mitterrand's principal advisers on economic affairs. Member of Management Committee of the PS since 1981. Appointed to present post May 1981.

Although a member of the Mitterrand faction, M. Delors is on the social-democratic wing of the PS. He is therefore suspect to his colleagues on the Left. But he retains M. Mitterrand's ear.

Delors is intelligent, hard-working and pleasant to deal with. His background is modest (he is of Christian trade union stock).

Married with 2 children. Has a slight knowledge of English.

Lord COCKFIELD

Vice President of the Commission – responsible for Internal market, taxation, financial institutions

Francis Arthur Cockfield. Born 28 September 1916.
Married Aileen Monica Mudie, choreographer. Created Life Peer 1978.

Graduate London School of Economics (LLB, BSc (Econ)). Called to the Bar (i.e. qualified as Barrister) 1942. Cabinet Minister since 1982. !!

Previous appointments: Home Civil Service, Inland Revenue 1938; Assistant Secretary to Board of Inland Revenue 1945; Director of Statistics and Intelligence to Board of Inland Revenue 1945-1952; Commission of Inland Revenue 1951-1952; Financial Director, then Managing Director and Chairman of Executive Management Committee, Boots Pure Drug Co 1953-1967; Member National Economic Development Council 1962-1964 and 1982-1984; Member, Court of Governors of University of Nottingham 1963-1967; President, Royal Statistical Society 1968-1969; Adviser on Taxation Policy to Chancellor of Exchequer 1970-1973; appointed Honorary Fellow, London School of Economics 1972; Chairman, Price Commission 1973-1977; Minister of State, HM Treasury 1979-1982; Secretary of State for Trade 1982-1983.

26

CHRISTOPHERSEN, HENNING   Since January 1985 Vice President of the Commission
Responsible for - Budget - Financial control
Personnel and administration

Finance and Deputy Prime Minister
September 1982 — 1984

Born 1939. Graduated in political science 1965. Head of the Industrial Economy Division of the Artisans Council 1965-70. Principal of a liberal 'high school' 1971-72. Subsequently an economic consultant for various organisations and an economic and political journalist for the leading weekly 'Weekendavisen'. Member of the Folketing since 1971. Deputy chairman of the Venstre (Liberal) Party Organisation from 1972-77, when he became provisional chairman on Mr Poul Hartling's departure. He was confirmed in office at the Party Congress in September 1978. Visited Britain as a FCO sponsored visitor 1975. Minister of Foreign Affairs 1978-80.

Although his previous experience was more with internal than external affairs he took the Foreign Ministry as the senior post offered to Venstre in the coalition Government formed in August 1978. Although not formally appointed Deputy Prime Minister, he deputises for the Prime Minister in the latter's absence. During the difficult early stages of the coalition, he had to give much of his attention to party and government business centering on domestic economic and financial issues. But his senior officials soon spoke admiringly of his rapid grasp of foreign affairs briefs. Venstre is the most pro-European of Danish political parties and Mr Christophersen takes a keen personal interest in work in Brussels as well as in political cooperation.

He displayed courage and political skill in bringing about a major realignment in policy within his party, and grew in public esteem during the negotiations for the formation of the coalition. The odds must be that he will be prominent on the Danish political scene for many years to come.

Personally friendly, with more than passable English. Married. His wife's sister is the widow of Sir Donald Hopson.

Vice President of the Commission
responsible for agriculture and forestry

ANDRIESSEN Frans H.J.J.

born on 2 April 1929 at Utrecht - Married: 4 children

1951	Degree in law at the State University of Utrecht;
1954 to 1972	Discharged various duties at the Catholic Institute for Housing (last position held: Director)
1958 to 1967	Member of the Utrecht Provincial States
1967 to 1977	Member of the Second Chamber of the States-General (specializing initially in matters relating to low-cost housing
1971 to 1977	President of the KVP Group of the Second Chamber
1977 to 1979	Minister for Finance
1980	Member of the First Chamber of the States-General (Senate)
6.1.81	Member of the Commission of the European Communities with responsibility for relations with the European Parliament and for the competition sector

Mr Andriesen is a knight of the Order du Lion Néerlandias and an officer of the Order of Orange-Nassau.

.../...

28

responsible for external relations
and trade policy

DE CLERCQ, WILLY
Member of the European Commission since Jan 1985

Former Deputy Prime Minister, Minister of Finance and Foreign Trade. Former President of the PVV. Former Minister of Finance in the 1974-77 Tindemans government. President of the Liberal group to European Parliament since 1981. Chairman of IMF's Interim Committee. ~~He is to be the next Belgian member of the European Commission.~~

Born 1927.

A brilliant student, and Doctor of Law summa cum laude. Studied at Syracuse, USA (MA in Social Sciences). He is a lawyer. He entered politics when he was very young, and became a town councillor of Ghent in 1952. He entered Parliament in 1958 and was elected leader of the PLP Parliamentary group after the elections of May 1965. In 1960 he was an Under-Secretary in charge of the Budget in the Eyskens government. He was Deputy Prime Minister in charge of the Budget under Vanden Boeynants and established a reputation as an able economist. In 1973 Leburton re-appointed him Deputy Prime Minister and Minister of Finance and he continued to hold the latter post during the Tindemans government (1974-77). During the Belgian EC Presidency in 1977 his handling of the Finance Ministers' meetings was much superior to the performance of his colleague, Foreign Minister Van Elslande. He enjoys considerable popular support in Ghent and was largely responsible for the PVV's gains in the communal elections of 1976. However, in the April 1977 national elections, De Clercq unexpectedly failed to be re-elected, partly because of the unpopular economic measures he had had to take as Minister of Finance, but, more importantly, because of his long-standing friendship with a local judge, who had shortly before the elections, been arraigned on corruption charges. He is considered to be a moderate Fleming and tolerant in his general outlook.

Friendly, speaks good English. His intelligent wife (also a lawyer) helped to run his chambers when he was a Minister, and is involved in PVV activities in the Ghent area.

Louvre agreement

Art [illegible] [illegible]

* Procedure / legal pos:

Intra marginal intervention (& VSTFF)

Contracts

Realignment procedure

[Margins]

£

"[illegible] rule"

What do we want to do?

Do it!

Move to complete capital liberalisation.

5. **General Government fiscal deficits (per cent of GNP)**

Signs ?!

	1986	1987	1988	
Belgium	-8¾	-6½	-6¼	
Denmark	3½	2½	2¾	
France	-3	-2¾	-2¾	
Germany	-1¼	-1¾	-2	
Greece	-10¼	-9½	-10¼	
Ireland	-10¾	-9	-7¾	
Italy	-11¼	-10½	-9¼	
Luxembourg	4	2½	2	
Netherlands	-6	-6½	-6	
Portugal	-8½	-9	-9	
Spain	-6	-5½	-5	
UK	-3¼	-2½	-2¼	1½
EC	-5	-4½	-4½	
US	-3¼	-2¾	-2	2¾
Japan	-1½	-1½	-1¼	

Source: EC Commission Forecasts, May 1987

6. **Money supply (change over previous period at annual rates)**

	1985	1986	latest growth over base at annual rate	Target range
Germany (CBM)	4.6	6.4	7.3 (Jul)	3 - 6
France (M3)	8.3	5.4	12.3 (Jun)	3 - 5
UK (MO)	4.6	4.0	5.4* (Jul)	2 - 6
US (M1)	9.2	13.4	10.5 (Jul)	na
Japan (M2+CDs)	8.4	8.6	10.3 (Jul)	10

* Change on level 12 months earlier.

7. **Three-month interest rates (per cent per annum)**

	1985		1986				1987		
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	1 Sept
France	9¾	9	8¾	7½	7¼	7¾	8¼	8	8
Germany	5	5	4½	4½	4½	4¾	4¼	3¾	4
Italy	14½	14½	15¾	12¾	11½	11¼	11½	10½	13
Netherlands	6¼	6	5¾	5½	5½	5½	5½	5¼	5¼
UK	11¾	11½	12½	10¼	10	11¼	10½	9¼	10½
Major EC average	9¼	8¾	9	7½	7½	8	7¾	7	7¾
USA	8	8	7¾	6¾	6¼	6¼	6¼	6¼	6¾
Japan	6¼	7	6	4¾	4¾	4½	4	3¾	3¾

We can settle for a
"bourse européenne".
It exists almost — in London.

GCl

DANMARK
1987

Agenda

Informal ECOFIN meeting in Nyborg

on 12 September 1987

Morning

1. Strengthening of the EMS and liberalization of capital movements. Reports from the Monetary Committee and the Committee of Governors of the Central Banks will be available.

Afternoon

2. Preparation for annual meetings of IMF and IBRD in Washington, including approval of Presidency's speeches. In this connection it would be useful to discuss the international economic situation and the proposed increase in the resources of the Monetary Fund's SAF facility.

Det økonomiske Sekretariat
Den 9. juli 1987

Dagsorden
Uformelt ECOFIN i Nyborg
Den 12. september

Formiddag

1. Styrkelse af EMS og liberalisering af kapitalbevægelserne. Der vil foreligge rapporter fra Den monetære Komité og centralbankchefkomiteen.

Eftermiddag

2. Forberedelse af Årsmøderne i IMF og IBRD i Washington herunder godkendelse af formandskabets indlæg. I denne forbindelse vil det være hensigtsmæssigt med en drøftelse af den internationale økonomiske situation og den foreslåede forøgelse af midlerne i Valutafondens SAF-facilitet.

PREPARATION FOR 14/15 SEPTEMBER FAC

6. AGENDA AS FOLLOWS:

- FUTURE FINANCING (RESTRICTED SESSION)
- EC/US - TRADE LEGISLATION (XX)
- (POSS) GSP 1988 (XX)
- (POSS) GATT ARTICLE XXIV.6 (XX)
- URUGUAY ROUND - TROPICAL PRODUCTS (XX)
- IAEA CONVENTIONS (XX)
- COMMUNITY RAPID NOTIFICATION SCHEME (XX)
- POST-CHERNOBYL RADIOACTIVITY IN FOODSTUFFS (XX)

(XX) POINTS ON WHICH A VOTE MAY BE CALLED.

OTHER BUSINESS

7. MONDAY 7 SEPTEMBER'S SPECIAL COREPER ON FUTURE FINANCING WILL CONCENTRATE ON

- GENERAL DISCUSSION OF THE COMMISSION'S PAPER ON REFORM OF THE STRUCTURAL FUNDS
- DRAWING UP A TIMETABLE OF SPECIAL COREPERS LEADING UP TO THE OCTOBER FAC. EACH COMMISSION PAPER WILL BE DISCUSSED OVER 2 MEETINGS. THERE WILL BE ANOTHER SPECIAL COREPER IN THE AFTERNOON OF TUESDAY 15 SEPTEMBER.

HANNAY

YYYY

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FRAME GENERAL

COREPER (AMBASSADORS) 3 SEPTEMBER 1987

SUMMARY
NB(X) DENOTES ITEM NOT REPORTED ELSEWHERE

COUNCIL MINUTES (X)
1. ALL CLEARED.

IAEA CONVENTIONS
2. FRENCH HINTED THAT THEY WOULD BE LIKELY TO AGREE TO EC ACCESSION TO THE CONVENTION ON RAPID NOTIFICATION ONCE THEY WERE SATISFIED ABOUT THE PARALLEL EC SYSTEM. NO PROGRESS ON MUTUAL ASSISTANCE CONVENTION. BACK TO COREPER ON 9 SEPTEMBER WITH A VIEW TO DISCUSSION AT 14 SEPTEMBER FAC.

COMMUNITY RAPID NOTIFICATION SCHEME (X)
3. GROUP MANDATED TO COMPLETE ITS WORK ON 4 SEPTEMBER AND REPORT TO COREPER ON 9 SEPTEMBER.

POST-CHERNOBYL RADIOACTIVITY IN FOODSTUFFS
4. PROTRACTED DISCUSSION OF MAIN OUTSTANDING POINTS. SOME HEADWAY ON PRODUCT COVERAGE (ANIMAL FEEDINGSTUFFS), WHETHER EXPORTS SHOULD BE COVERED, AND COMITOLOGY. COREPER TO RESUME DISCUSSION ON 9 SEPTEMBER TO PREPARE FOR 14 SEPTEMBER FAC.

PREPARATION FOR 21 SEPTEMBER INDUSTRY COUNCIL
5. AGENDA AS FOLLOWS:
A) STEEL POLICY AFTER 1987
- NEW ARTICLE 58 QUOTA REGIME, INCLUDING RESTRUCTURING SCHEME
- REGIONAL MEASURES (RESIDER PROGRAMME)
- SOCIAL VOLET
B) (POSS) TEDIS
COUNCIL TO START WITH LUNCH (IN VIEW OF CLASH WITH INFORMAL ENERGY MINISTERS' MEETING IN COPENHAGEN).

ITEM SHOULD NOT BE TAKEN UNTIL AFTER THE ARTICLE 113 COMMITTEE MEETING ON 8 SEPTEMBER. HE AGREED TO LET THE PRESIDENCY KNOW THE COMMISSION'S ATTITUDE ON THE EXCLUSION OF BOTH SUBJECTS AS SOON AS POSSIBLE.

EC/GCC

5. EC/GCC HAS BEEN DROPPED FROM THE AGENDA SINCE THE COMMISSIONS PROPOSALS WILL NOT BE READY UNTIL 16 SEPTEMBER.

IAEA CONVENTIONS

6. ESPER LARSEN WONDERED WHETHER THE MUTUAL ASSISTANCE CONVENTION SHOULD BE ON THE AGENDA, GIVEN THE LACK OF MOVEMENT IN THE FRENCH AND LUXEMBOURG POSITIONS.

LUNCH

7. TOPICS FOR LUNCH MAY INCLUDE THE MOROCCAN LETTER OF APPLICATION AND THE EUROPEAN FOUNDATION. BOTH WILL BE CONSIDERED AT COREPER LUNCH ON 8 SEPTEMBER.

HANNAY

YYYY

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FRAME GENERAL

COREPER (AMBASSADORS) 3 SEPTEMBER 1987
PREPARATION FOR 14 SEPTEMBER FOREIGN AFFAIRS COUNCIL

1. AGENDA AS FOLLOWS:
- FUTURE FINANCING (RESTRICTED SESSION)
- EC/US - TRADE LEGISLATION (XX)
- (POSS) GATT ARTICLE XXIV.6 (XX)
- (POSS) GSP 1988. (XX)
- URUGUAY ROUND - TROPICAL PRODUCTS (XX)
- IAEA CONVENTIONS - COMMUNITY ACCESSION (XX)
- COMMUNITY RAPID NOTIFICATION SCHEME IN THE EVENT OF A NUCLEAR ACCIDENT (XX)
- POST-CHERNOBYL-RADIOACTIVITY IN FOODSTUFFS (XX)

(XX) POINTS ON WHICH A VOTE MAY BE CALLED.
THE PRESIDENCY HAS NOT YET DECIDED WHEN THE COUNCIL WILL START.

FUTURE FINANCING

2. THE PRESIDENCY DOES NOT INTEND THAT THIS ITEM (WHICH IT REFERS TO AS ''THE COPENHAGEN DECISIONS'') SHOULD BE DISCUSSED IN SUBSTANCE. HOWEVER, THERE MAY BE PROCEDURAL QUESTIONS TO RESOLVE FOLLOWING THE SPECIAL COREPER ON 7 SEPTEMBER AND DELORS MAY WANT TO PRESENT THE PROPOSALS PREPARED BY THE COMMISSION SINCE THE JULY FAC.

EC/US

3. ESPER LARSEN (PRESIDENCY) SAID THAT, ALTHOUGH THE PASTA ISSUE WAS NOW SETTLED, THIS ITEM SHOULD BE RETAINED SINCE THE COUNCIL MIGHT WISH TO REAFFIRM ITS VIEWS ON THE US TRADE LEGISLATION AS STATED AT THE JUNE AND JULY COUNCILS. DE CLERCQ (COMMISSION) MIGHT ALSO WISH TO COMENT ON OTHER PROBLEMS ON THE HORIZON.

GATT ARTICLE XXIV.6 AND GSP 1988

4. THE PRESIDENCY CONSIDER THAT THESE SUBJECTS ARE NOT RIPE FOR DISCUSSION BUT SHOULD BE TAKEN AT THE OCTOBER FAC. KRENZLER (COMMISSION) ASKED THAT A DECISION ABOUT WHETHER TO DELETE THE GATT

Ch
This doesn't seem v satisfactory.
I have brought forward Wattenberg
wk Geoff to the PM.
AA

From: Sir G.Littler
Date: 3 September 1987

CHANCELLOR

c.c. Mr Lavelle
Miss Barber

INFORMAL ECOFIN

Two things I gleaned at yesterday's Monetary Committee meeting in relation to next week's informal ECOFIN.

Balladur/Stoltenberg

?? It was much more than that

2. You will remember a casual suggestion by Balladur at your meeting with him on 31 July, that you and he (and ? Stoltenberg - I was unclear whether bilateral or trilateral was implied) might meet together in Denmark just before the informal ECOFIN. It is clear that this cannot be fitted in. I learned that a postponed Balladur/Stoltenberg bilateral has now been refixed for Bonn next Friday on the way to Denmark; they are unlikely to reach Nyborg much before 6 p.m., which leaves no time for a meeting there before the general reception and dinner.

3. This suggests we stick to your present flight-plan, getting us to Nyborg around the same time as the others.

Tax Approximation

4. My Danish colleague confirmed that the agenda in Nyborg will cover only two substantive items (he circulated the attached note), and that tax will not be discussed. Tietmeyer told me that Stoltenberg has two pre-occupations outside this agenda:

- tax approximation: which he may well want to mention at the meeting, although only on a procedural level. I asked whether he had any procedure in mind: Tietmeyer said he did not at present but was worried about how to get into such a delicate subject and make progress in discussion with other Ministers without arousing premature public interest and debate. I suggested, and Tietmeyer warmly agreed, that you and Stoltenberg might usefully try to have a chat together about this on Friday evening, so that you could concert remarks at the meeting if that appealed to you both;

- the Community Budget: on which Stoltenberg is worrying about costs to the FRG and Tietmeyer warned me that an element of this is the UK refund, but added that he did not himself see the way forward on this either!

(Geoffrey Littler)

Agenda

Informal ECOFIN meeting in Nyborg

on 12 September 1987

Morning

1. Strengthening of the EMS and liberalization of capital movements. Reports from the Monetary Committee and the Committee of Governors of the Central Banks will be available.

Afternoon

2. Preparation for annual meetings of IMF and IBRD in Washington, including approval of Presidency's speeches. In this connection it would be useful to discuss the international economic situation and the proposed increase in the resources of the Monetary Fund's SAF facility.

FROM: I C R BYATT
DATE: 4 SEPTEMBER 1987

MISS BARBER

c PS/Chancellor
Sir G Littler
Mr Lavelle
Mr A Edwards
Mr H P Evans
Mr Bonney
Mr G White
Mr Corry
Ms Symes
Mr Westcott (UKREP)

INFORMAL ECOFIN: AGRICULTURE

At the meeting which the Chancellor held on agriculture on 3 August 1987, I agreed to speak to Mr Milleron to see whether the French intended to ask for a discussion of the paper which the EPC wrote on agriculture at a meeting of Ecofin.

2. I have spoken to Mr Milleron, who in turn has consulted Mr Balladur's Cabinet. They think the paper is a good one, but they do not want to press for a formal Ecofin discussion on it at this stage. This is partly in order not to confuse the current negotiations, but also because they do not want a public argument with the French Minister of Agriculture.

3. Instead, they suggest that the Chancellor and Mr Balladur should discuss the matter in the margins of the informal Ecofin next week. The EPC paper will be in Mr Balladur's briefing, together with the suggestion that he should talk to the Chancellor about the matter.

4. I have also tried to talk to my opposite number in the Hague, as the Dutch were keen to get a good paper on agriculture at the EPC meetings. He is on holiday this week, but returns on Monday and I will encourage him to encourage his Minister to raise the matter with Mr Balladur. This seems the right way round as the EPC Chairman is a Frenchman.

5. When the Chancellor talks to Mr Balladur, I suggest he should aim to persuade him that it is necessary for Finance Ministers to take an active role at a Community level in agricultural matters, in part because of the budgetary consequences of the CAP and in part because of the wider damage present policies are doing to the economy via higher prices for consumers and damage to world trade generally. The particular points which the Chancellor might like to make in such a discussion are:-

(i) The agricultural issue is already serious and shows signs of deterioration. Agricultural productivity is likely to continue to rise more rapidly than the demand for food.

(ii) The CAP has already produced adverse consequences for budgetary discipline in the Community. It raises food prices and produces trade problems. It is a negative sum gain.

(iii) Eventually, there is no substitute for lower prices. We need to establish policies that work with the grain of market forces.

(iv) In the meantime, we must pursue the stabilizers, especially those which can limit Community expenditure - e.g. suspension of further support if the budget limit is reached.

(v) Indicate willingness to agree to income aids if inextricably linked to price reductions.

6. I would be grateful if you could incorporate these points in briefing for the Chancellor. I will let you know what I get out of the Dutch.

ICR Byatt

for I C R BYATT

10/4

CONFIDENTIAL

Miss Noble is preparing a text.

Ch,
Content to speak to Stoltenberg as suggested? AS

FROM: MISS G M NOBLE
DATE: 9 September 1987

CHANCELLOR

Wd it not be better for me to write to Stoltenberg on so technical a theme? I cd then hand him the letter + say words in support of it. N

c c Economic Secretary
Sir P Middleton
Sir G Littler
Mr Cassell
Mr Lavelle
Mrs Lomax
Mr Edwards
Mr Mortimer
Mr Board
Miss Barber

CAPITAL CONVERGENCE : INFORMAL ECOFIN 11-12 SEPTEMBER

We think it would be helpful if you could have a private word with Stoltenberg in the margins of ECOFIN, to encourage the Germans to take a more positive role in the discussions on convergence. (The Bank agree and this submission has been cleared with them.) The Germans have been unhelpful to date and their co-operation is important. There is a crucial meeting of the Basle supervisor's committee on 16-18 September. If substantial progress is not made at that meeting, then at best the timetable will be put in jeopardy, and at worst the whole convergence exercise could start to unravel.

Background

2. You are familiar with the background to this issue. As you know, the Basle group's meeting in June ran into some difficulty, mainly over the definition of capital. The Germans pressed for a very narrow definition, partly because that is what is incorporated in their recent banking legislation which they are obviously reluctant to change, and partly because they believe quite strongly that their definition is conceptually right.

3. The issue was discussed again at the G10 Governors meeting in July and rather more progress was made. In particular, the Governors firmly, and unanimously, endorsed the aim of reaching

agreement by the end of the year; the Cooke Committee were instructed to produce a firm basis for agreement for the Governors to consider at their meeting in November, with the aim of publishing a definitive and agreed paper by Christmas.

4. The Bank believe they now have the basis for a compromise which the Germans, and the fact that the Germans endorsed the timetable should mean there is no problem. But there is a separate difficulty that the Basle committee is a group of central bankers, whereas, in Germany, banking supervision is the responsibility of the Ministry of Finance (through the Federal Banking Supervisory Office). And the Ministry of Finance are proving even more negative than the Bundesbank. They take the lead in the parallel discussions on banking supervision in the EC, where the key proposal - the "own funds directive" - which will determine the definition of capital for the EC purposes, is closest to adoption. The discussions of this directive in the Council working group have been largely preparatory so far, but the Danish Presidency has made it clear that they intend to make rapid progress on it during this autumn. While virtually everyone else, including the Commission, recognise the need for consistency and accept that it makes sense for the Cooke Committee to make the running in drawing up the framework for a common agreement, the Germans have been unenthusiastic in the EC discussions (often explicitly so) about the two groups proceeding on a common path. Their main argument is that the Basle group has no legislative responsibility; but they have also argued that Basle is primarily concerned with international banking, whereas EC banking legislation covers all sorts of banks.

5. It is not clear how much of the problem is a lack of communication between the Bundesbank and the Ministry of Finance on the objectives and importance of the convergence exercise (or perhaps just institutional rivalry between them), and how much is due to the underlying, conceptual difference of approach and an understandable reluctance to change legislation which has just been put in place. But what is clear, is that if the German negotiators (particularly those in the Ministry of Finance) are not given a firm political steer about the need to reach agreement,

they could put the Cooke timetable, and the whole convergence initiative in jeopardy. (We will get into particular difficulties if the "own funds directive" goes off on a significantly different tack from any agreement we could hope to reach with the Americans or Japanese, especially when the Germans take over the Presidency in January).

Recommendation

6. You will have your own views on how best to handle this. But, if you agree, the message we think it would be most useful to give Stoltenberg (which has been cleared with the Bank) is:-

- You attach great importance to the success of the current discussions aimed at securing convergence of capital adequacy requirements in both the EC and G10 countries. To include the USA and Japan in an agreement would be a major prize, which is well within our grasp if enough political weight is put behind it.

- Germany's support is especially important. You hope Stoltenberg will do everything he can at his end to see that this major opportunity is not missed.

- You understand there have been particular problems over the definition of capital, but that the Bank believe they have identified a basis for compromise (which gives due prominence to a very narrow definition of top quality capital). You are sure any remaining problems can be sorted out, given enough will; and you hope German officials will get in touch with the Bank if there are any difficulties to try to sort them out on a bilateral basis.

- Time is short. The next few weeks, but especially the Basle supervisors committee meeting on 16-18 September and EC Council working group discussions on the "Own Funds Directive" will be vital if the USA and Japan are to be included in an agreement by the end of the year.

7. If you are content, we will include this in a self-contained aid-memoire in your brief for ECOFIN.

G M Noble

MISS G M NOBLE

ECON POL REP ON CAP 9

V3875.04

ANNEX G

INFORMAL ECOFIN: 11-13 SEPTEMBER 1987

(For discussion in the margins with M.Balladur)

ECONOMIC POLICY REPORT ON THE CAP

Relevant document: EPC Chairman's Report (attached)

UK Objective

To probe M.Balladur's willingness to promote ECOFIN discussion of EPC report on the CAP in due course.

Line to take

- EPC Report useful general analysis of budgetary and other problems arising because CAP not sufficiently subject to market forces: and how to approach reform

- French provided Chairman for the Group. How do they see future handling of report, including timing of ECOFIN discussion?

Background

The Economic Policy Committee (EPC) has recently been considering the Community's agricultural policy and its Chairman, M.Milleron, has now produced a report. (The report has been circulated to EPC members. We expect that it will be formally submitted to the Council this month, but this has not yet been done).

2. We would like the report to be discussed by ECOFIN provided we did not appear in the lead or use up political capital in pressing for it. But the French (who would be best placed to ask for an ECOFIN discussion as the EPC Chairman is French) do not want to press for one at this stage on the grounds that this might confuse the on-going negotiations and reveal differences of view between French Departments. However, it is being suggested by French officials to M.Balladur that he discuss the matter with you in the margins of this informal ECOFIN. We understand that the Dutch also like the EPC report and that Mr Ruding may also speak to M.Balladur with a view to encouraging some involvement for Finance Ministers in the issues raised by it.

9

3. Once the report has been discussed in ECOFIN it would also be possible to make general public use of the points in it - eg in speeches.

4. The EPC report (attached) argues that, with prices maintained above equilibrium levels, and as food surpluses have built up, the CAP has led to budgetary, resources allocation and trade problems. Reform needs to address all of these. Its main thrust should be internationally concerted action on a gradual basis. As well as reductions in support prices, it may be necessary to make use during the transitional period of other measures, such as limitation of intervention obligations, co-responsibility levies, quotas, or setting aside of land. It may also be necessary for these measures to be accompanied by policies to improve factor mobility (eg training, and conversion aids), by income support (other than via pricing), and by policies to improve agricultural structures where this is consistent with reducing distortions and environmental and other new objectives.

COMMUNAUTES EUROPEENNES
Secrétariat du Comité
de Politique économique

EUROPEAN COMMUNITIES
Secretariat of the
Economic Policy Committee

EUROPÄISCHE GEMEINSCHAFTEN
Sekretariat des Ausschusses
für Wirtschaftspolitik

Brüssel, den

14.08.87 /II/05492

VERMERK AN DIE MITGLIEDER DES AUSSCHUSSES FÜR WIRTSCHAFTSPOLITIK

Beiliegend erhalten Sie die endgültige Fassung des Berichts zur Agrarpolitik der Gemeinschaft, wie sie auf der Tagung am 8. Juli 1987 offiziell angenommen wurde. Der Präsident wird diesen Bericht Anfang September dem Rat übermitteln.

NOTE A L'ATTENTION DES MEMBRES DU COMITE DE POLITIQUE ECONOMIQUE

Veuillez trouver, ci-joint, la version definitive du rapport sur la politique agricole de la Communauté telle qu'elle a été officiellement adoptée lors de la réunion du 8 juillet 1987. Le président transmettra au début du mois de septembre ce rapport au Conseil.

NOTE FOR THE MEMBERS OF THE ECONOMIC POLICY COMMITTEE

Please find enclosed the final version of the report on the Community's agricultural policy which has officially been adopted at the meeting of 8 July 1987. The chairman will transmit this report to the Council at the beginning of September.

A. Kees

EUROPEAN COMMUNITIES
ECONOMIC POLICY COMMITTEE

The Chairman

Brussels, 8 July 1987

ECONOMIC REFLECTIONS
ON THE COMMUNITY'S AGRICULTURAL POLICY

REPORT TO THE COUNCIL

The Economic Policy Committee sees it as one of its tasks to take a position on pressing questions of economic policy in order to assist and orient policy-makers in their decisions. It therefore considers it appropriate to comment on agricultural policy from a general economic point of view. It is clearly not the business of the Committee to present detailed specific proposals for the reform of the Common Agricultural Policy.

The Committee has asked me to report to the Council (Economic and Financial Affairs) on the outcome of its dicussions on agricultural policy. This could be useful in view of the deliberations on this matter which will follow the European Council of the end of June 1987.

*

* *

The current situation and fundamental problems

1. The Common Agricultural Policy (CAP) has certainly achieved most of the aims listed in the Treaty of Rome. But in recent years it has itself resulted in serious imbalances. As long as the Community had a shortage of most of the main agricultural products, supporting farm incomes via prices - the salient feature of the CAP - meant that the cost was paid for essentially by the consumer. This helped to disguise budgetary and other problems. As the Community became increasingly self-sufficient in food, however, substantial production surpluses also came into existence since year

by year supply was on average increasing far more sharply than demand. This led to the build-up of huge stocks, placing an ever-heavier burden on the Community budget. The CAP also led to a distorted allocation of economic resources and intensified certain trade conflicts. At the same time it still failed to prevent large sections of the agricultural population from regarding their incomes as unsatisfactory. Besides the Community, almost all the other industrialized nations share responsibility for the present situation on the agricultural markets. World-wide protectionism in agricultural policy led to a collapse of world market prices and to distortions in international agricultural trade.

Budgetary and macroeconomic aspects

2. It is true that reform of the CAP has become a pressing need as a result of the high costs and the financing difficulties besetting the Community budget. However, reform should not be confined to this one aspect of the situation, however important it may be. It should be geared to reducing progressively the present distortions without at the same time creating new ones.

3. Prolonged maintenance of support or guarantee prices above their equilibrium level has the effect of retaining too many workers and too much capital in agriculture and produces excessive costs for the other sectors of the economy. This results in distortions between agriculture and these other sectors. Moreover, if some products are afforded greater protection than others, it also results in distortions even within agriculture.

4. When agricultural prices are held above equilibrium levels, they also directly impair the competitiveness of the industries processing agricultural products. High prices and support costs place a burden on other sectors, reducing the competitiveness of the economy as a whole. As a result of the

wider effects of agricultural protection on international trade, agricultural policy has also had an adverse effect on producers of other tradeable (especially manufactured) goods.

Guidelines for reform

5.- The main pillar of the reform of the CAP must be to make agriculture once more subject to the rules of the market economy. Prices which do not reflect the market situation give rise to the misallocation of resources. This is why genuine market signals must again, and to an increasing degree, determine farmers' decisions, and the conditions for this must be established. Price policy should not be the only tool of ensuring proper incomes for those engaged in agriculture. A more market-oriented policy is needed to bring about a balanced relationship on a lasting basis between the supply of and demand for agricultural products and the more efficient allocation of resources. Such a policy requires certain transitional arrangements and should be accompanied by appropriate socio-structural measures.

The adjustment process

6. The existing imbalances have built up over a long period. They are so great that they cannot be corrected in the short term. Because prices on world agricultural markets have been distorted by manifold interventions, internationally concerted action is necessary so that the conditions for market equilibrium can gradually be restored. The distorting elements of the policy of agricultural intervention must be eliminated step by step. This applies to the Community but also to other countries which determine world trade in agricultural products.

7. The reform of the agricultural policy will require an adjustment process stretching over several years. During this phase it will very probably be difficult to avoid measures working in the same direction as the necessary shift of

official prices such as a limitation of intervention obligations and the introduction of co-responsibility levies. In cases where supply takes too long to respond to the gradual adjustment of prices, and surpluses build up, temporary recourse to instruments of administrative control may be justified, such as measures restricting the output of products qualifying for price guarantees (quotas), or the use of certain factors of production (setting aside of land). In doing so, special situations in Member States should be taken into account.

8. When products are subjected to quotas, a gradual alignment of producer prices on equilibrium prices is also necessary. Views differ on the most appropriate way to relate the process of price adaptation to the phasing out of quotas.

The policy of setting farmland aside requires the utmost caution because it distorts factor prices. It boosts the value of the agricultural land which is allowed to be used and prevents land from being used for alternative purposes (agricultural or otherwise). It can also lead to more intensive use of the land remaining in production, and partly frustrate the objective of reducing production.

9. As regards the adjustment of prices, two further considerations should be taken into account:

On the one side, it would be desirable gradually to harmonize the degree of protection enjoyed by the various agricultural products, so as to reduce the distortions within the agricultural sector. This would mean that, as far as possible, the most heavily protected products should be dealt with first.

On the other side, price differences resulting from monetary compensatory amounts should be gradually reduced and disappear altogether with the completion of the internal market. The European Council has introduced a system which goes in this direction.

Social and structural policy

10. The reform of the CAP by a gradual transition to a policy more reliant on market forces must be accompanied by measures, dealing with the following in particular :

- greater mobility of the factors of agricultural production;
- social welfare measures to support this reorientation;
- an appropriate policy on agricultural structures.

The Comittee is aware that structural adjustment in agriculture, as in other sectors of the economy, is easier to undertake in an environment of economic growth and high employment.

a) Factor mobility

11. Labour mobility could be encouraged by an improved training policy, backed up by appropriate aid for conversion and restructuring. These aids should not, wherever possible, be linked to the quantities produced, or to farm inputs. They need not depend on whether or not the farmer leaves the sector. Non-agricultural jobs should be created by encouraging the expansion of other industries or services.

Moreover, care should be taken to ensure that there is no further distortion of relative factor costs in the agricultural sector and that there are no artificial and short-sighted incentives favouring the use of capital rather than labour, such as aids to investment or for the more intensive use of land following set-asides.

b) Aids of a social nature

12. The Committee acknowledged the value in principle of such aids for an appropriate transitional period. Aids should be person-related. The basis for determining aid should be the total income of persons employed in agriculture (including subsidiary earnings) and not only their income from agricultural activity. The Committee felt that it is not part

of its remit to express a detailed view on the manner in which, or the level at which, such aids could be granted. Given the diversity of farmers' situations in the Community, implementation by national authorities within a Community framework would be most appropriate. This should not be seen as a step towards the renationalisation of the CAP. These measures should not be such as to increase agricultural output.

c) Policy on agricultural structures

13. Policy on agricultural structures should, as a general rule, be designed to be consistent with a policy directed towards reducing distortions and surpluses. Above all it should not encourage investments designed to increase production when this is inappropriate. This basic stance should not rule out social or other policy measures insofar as these seem necessary for reasons to do with the structure of society, the environment and regional development. In this context, the Comittee pointed to the need to take account of the problems of regions which would be particularly affected by the adjustments in agriculture.

Incorporation of new objectives

14. In recent years, increasing importance has been attached to concerns such as the protection and improvement of the environment and of landscapes. In these respects farmers may perform a service to society without receiving payment via producer prices. New tasks could properly be defined for them for which they would be paid - insofar as this is not already the case. Compensation could be envisaged in cases where the permanent abandonment of farmland or its conversion to other uses is entailed. If, for ecological reasons or for the purposes of landscape improvement, it seems desirable to preserve agricultural activities in specific areas, provision should be made for the appropriate measures.

15. In order to prevent over-intensive use of the soil, ecologicially undesiderable production methods, the inadequate rotation of crops or high-density stockfarming from entailing risks and costs to the environment, the same principles should as far as possible be applied to agriculture as are applied in environmental policy generally, among which the principle that "the polluter pays" plays a key role.

Summary

16. The main considerations are the following:

- It is essential to obtain a better adjustment of supply to demand through measures enabling the market to play a greater role.

- A more strongly market-related pricing policy should be the central pillar of the reform of the CAP. In particular, pricing policy must gradually be detached from the objective of income support; other instruments should be used to ensure proper incomes for those engaged in agriculture. Prices should again be more strongly determined by the aim of balancing supply and demand than they are in the present system. This would help to ensure the better allocation of resources whilst reducing the overall budgetary burden. It can only be brought about by an adjustment process stretching over several years.

- Since the reorientation of agricultural policy requires radical adjustments on the part of farmers, it requires corresponding back-up measures. These could in particular comprise aids for restructuring and conversion as well as social measures, the overall budgetary costs of which should be lower than the savings obtained by the price reductions.

- New or broader tasks in the field of environmental and landscape protection and improvement might provide employment and reduce the extent of the necessary structural adjustment.

- World agricultural markets are at present characterized by distortions caused by various interventions in most countries. The progressive removal of interventions which work against a more balanced relationship between supply and demand is thus also a matter for international negotiations and will call for contributions from all participating in them.

EC PROP TAX APPROX
H

ANNEX H

ECOFIN: 11-13 SEPTEMBER 1987

COMMISSION PROPOSALS FOR TAX APPROXIMATION

Relevant documents: Proposals summarised in Global Communication from the Commission (COM 87 320 final). (copy attached)

UK objective: Defer procedural (or substantive) discussion of the tax approximation proposals. Discussion at this meeting (if any) will be introductory and general

Line to take: [If discussion arises]

- UK agree that Commission's proposals need proper consideration by Council. October ECOFIN appropriate venue for procedural discussions.

- Commission Proposals have far-reaching implications for all Member States. Much consideration will be required in the months ahead.

- UK fully committed to completion of the internal market.

- UK will work to find practical and pragmatic solutions.

Background: Cockfield's package of proposals approved by Commission 15 July and submitted to Council 7 August.

At informal ECOFIN in April, Germans proposed preliminary discussions in September and procedural discussions in October. Danes not keen to see proposals pushed forward and have excluded approximation from September agenda. October ECOFIN may nevertheless consider handling of the proposals, with detailed technical discussion beginning October/November.

Mr Knox's note of 4 September outlined main areas of difficulty; and suggested alternative approach based on real reductions in data requirements in context of border controls (copy attached).

H

ds5

Annex B3

B3

FROM: D SAVAGE
DATE: 9 September 1987

MR BATT

cc: Mr Evans
Mr Matthews
Mr Walsh
Miss Barber 20/G
Mr Dolphin
Mr Colenutt
Mr Drummond - FCO
Mr Jenkinson - BoE

BRIEFING FOR 1987 ANNUAL MEETINGS

I attach:

a. A brief on the World Economic Outlook, which is based heavily on the briefing for the Executive Director's discussion of the WEO. The usual statistical tables to follow.

b. A background brief on the US economy. (The figures for interest rates and exchange rates will need updating.)

DS.

D SAVAGE

international monetary system, especially because it was backed up by domestic policy commitments.

As was stated in the Paris meeting, a precondition for exchange rate stability and more balanced global growth is that the policies announced by the major countries be fully implemented and that economic policy coordination be intensified. In this context we welcome the greater use of indicators as an instrument of multilateral surveillance to promote international economic policy coordination.

4. In parallel with the international efforts to achieve a higher degree of exchange rate stability, at the European level we are proceeding in our endeavours to strengthen monetary cooperation within the EMS. We feel that developments since early 1987 have been satisfactory, and we are presently seeking ways to improve our cooperation in the monetary field even further. In line with the approach followed within the IMF and with the declaration adopted at the World Economic Summit in Venice in June we also are planning to make increased use of indicators in our internal surveillance activities aimed at improving the convergence of economic fundamentals within the Community.

5. We find developments so far in the Uruguay Round satisfactory, but much needs to be done to conclude the preparatory phase successfully by the end of this year. The European Community intends to participate constructively in these negotiations.We are very concerned about the pressures for increasing protection while the trade negotiations are still in progress. One particularly difficult and sensitive subject in this context is the question of international trade in agricultural products. Almost all countries bear some responsibility for current problems. Within the European Community we are aware of our responsibilities in this field.

MONETARY COMMITTEE

OF THE EUROPEAN COMMUNITIES

Brussels, 7 September 1987

II/328/87 - Rev. 1

DRAFT STATEMENT BY MR PALLE SIMONSEN,
CHAIRMAN OF THE COUNCIL OF THE EUROPEAN COMMUNITIES,
TO THE IMF/IBRD ANNUAL MEETINGS OF SEPTEMBER 1987

1. Since Denmark currently holds the Presidency of the Council of the European Communities, I have the honour to address you in the name of the Member States.

2. World economic developments over the last 12 months have not lived up to initial forecasts. In the course of the winter 1986/87 there were signs of weakening in demand and production in several industrialized countries. A clear sense of uncertainty was noticeable during this period, which, if sustained, would likely have negative effects on the world economy.

However, we are confident that both demand and production are now again on an upward trend. Although the decline in energy prices has been partially reversed in 1987, we think that price developments so far have been encouraging. Nevertheless, it is worrying that, both within the European Community and in most other industrialized countries, we are still faced with a rate of unemployment which is too high, with a rate of new productive investment which is still inadequate and with large current account imbalances in the major industrial countries, which are, however, declining in real terms.

3. Against the background of the very substantial adjustment of exchange rates which took place in 1985/86, the agreement reached in Paris in February, which was subsequently supported by the April meeting of the Interim Committee of the IMF and by the Venice Summit in June, proved timely and successful. It has contributed to a better functioning of the

Primary product exporters, and particularly those dependent on a single commodity, deserve special consideration and it may be appropriate to make adequate resources available to them on concessional terms.

9. As far as the middle-income debtors are concerned there have been further useful innovations broadening the range of procedures and financing techniques by commercial bank creditors which hopefully will facilitate the assembling and implementation of financial packages. However, the process of normalizing debtor/creditor relations so as to regain normal market access is ineviably taking a long time. Although progress has been made in several countries, in some debtor countries the perseverance in adjustment policies has not always measured up to what is needed, and financing flows to the developing countries have fallen short of expectations.

All parties involved must make further progress in a cooperative spirit for the full implementation of the debt strategy, with the vital support of private financing, both by the banks and in the form of non-debt creating capital flows to debtor countries.

10. The Member States of the Community continue to take the view that the resources of the IMF should predominantly come from quota subscriptions. For the IMF to be able to continue to play a central role both in the adjustment process and as the global monetary institution it will be important that the Fund has sufficient usable resources. Therefore, we welcome that the Executive Board has initiated discussions on the Ninth General Review of Quotas, in which the Member States of the EC will participate constructively.

11. The Member States of the Community adhere to the view that the Fund's Enlarged Access Policy is a temporary facility. However, in view of the continued payments imbalances and difficulties in several member countries we are prepared to support a continuation of that policy for 1988.

6. We welcome the satisfactory conclusions of UNCTAD VII, which have led to a common evaluation of the international economic situation and to a willingness to strengthen the efforts of the international community.

7. Turning now to the debt strategy, the Member States of the Community remain committed to the case-by-case approach which assures the best possibilities of taking into account the special circumstances of different indebted countries. While this strategy has served all the parties concerned well, it has also for some time been evident that it needs reinforcement and that all its elements have to be implemented more effectively.

8. Viewed against this background, some positive developments have taken place since the meeting of the Interim Committee in April this year, in particular in regard to the poorest countries, and among these primarily the Sub-Saharan African countries, for which the outlook remains bleak. Intensified deliberations in the Paris Club have already resulted in longer repayment and grace periods with respect to rescheduled official credits for certain countries in support of their far-reaching economic reforms. Proposals for lower interest rates have been put forward.

An important new development is the proposal by the Managing Director of the IMF for a substantial increase in the resources of the Fund's Structural Adjustment Facility (SAF) over the three-year period 1988-90, to be associated with the adoption of strong growth-oriented adjustment programs by low-income countries in close collaboration with the World Bank.

The Member States of the Community welcome the principles underlying these proposals and, despite some difficult issues which are not all purely technical, share the willingness to conclude discussions on these proposals by the end of this year. In the context of this facility, collaboration between the IMF and the World Bank will be important for the envisaged catalytic role of the facility to materialize.

The Member States of the European Community also look forward to the results of the ongoing review of the Compensatory Financing Facility.

12. Over the past couple of years there has been an increasing cooperation between the IMF and the World Bank in particular with respect to the poorest developing countries in solving their economic problems.

A situation where the needs of the developing countries are increasing rather than decreasing and where World Bank lending is approaching the statutory limits, underlines the need for an early agreement on a general capital increase.

13. An important contribution to easing the problems of the poorest countries should also come from the high level reached for IDA 8. We therefore hope that it will be possible for donor governments to complete rapidly their domestic procedures to ensure a timely implementation of the replenishment.

14. The Member States of the European Community feel strongly that special and innovative measures are called for to help debt-distressed countries in Sub-Saharan Africa undertaking rigorous policy reform. The World Bank together with the IMF has an essential role to play in promoting and coordinating these measures. We therefore welcome the increased emphasis on these issues as recently reflected in the Bank's proposal for a Special Action Program aimed at a concerted effort for additional financing from the donor community in order to assist the sub-Saharan countries' own efforts in tackling their problems.

15. The EC-countries hope that the requisite number of ratification instruments will be deposited soon to allow MIGA to enter into force. We are convinced that this new arrangement will play a beneficial role in promoting and supporting foreign direct investment.

HER MAJESTY'S TREASURY

BRIEFING FOR THE 1987 ANNUAL MEETINGS OF THE IMF, IBRD AND COMMONWEALTH FINANCE MINISTERS

WORLD ECONOMIC OUTLOOK

OBJECTIVES

1. Agree with IMF staff assessment that momentum of output growth in major countries will be reasonably well maintained in the short term, in the absence of any major shocks, although growth may fall short of potential in some countries.

2. Agree that projected current account imbalances are major cause for concern and that macroeconomic policies in the US, Japan and Germany should aim to achieve growth rates of domestic demand relative to productive potential that would reduce them. Credible action to reduce US Federal budget deficit in FY1988 remains central to any co-operative strategy. Exchange rate changes alone would not achieve the necessary adjustment. [illegible], not clear Reagan would.

3. Emphasise importance of sound adjustment policies for all debtors, but note their heterogeneity. Encourage international support for Chancellor's Sub-Saharan Africa initiative, especially given gloomy prospects for this region.

4. Stress importance of structural reforms for improving economic performance of industrial and developing countries.

5. Emphasise costs to all of increased protectionism. Regret trend toward bilateralism in trade questions.

POINTS TO MAKE

On Industrial Countries

1. External imbalances of three largest economies pose chief threat to sustainability of growth. Given present size of US deficit and Japanese and German surpluses, and what we know of elasticities, cannot expect exchange rate changes alone to correct imbalances over a reasonable time scale. Hence need to focus on relative growth rates of domestic demand.

2. It is essential in this connection that, as the US undertook in Paris in February, its fiscal deficit be reduced. Note some increase is expected in FY1988 due to one-off nature of additional revenues from tax reform in 1987.

3. Japan and Germany should, in accordance with their Louvre commitments, pursue policies to strengthen domestic demand and be prepared to re-examine their policies if the intended strengthening does not materialise. Hope that Japanese package is as large and stimulative as it has been presented. Germany should implement the tax cuts planned for 1988 and for 1990. Structural reforms would also help to promote domestically-generated growth in Japan and Germany. Japan should implement, as soon as possible, recommendations of Maekawa Commission. Germany should cut subsidies to declining industries.

4. Major objective of macro policy remains containment of inflation. Benefits of enhanced credibility have been hard won and should not now be thrown away. However countries where inflation is now very low should seek to sustain growth of money demand at rate sufficient to allow output to expand at (or, if there is slack, for a time above) productive potential.

5. Stress urgent need to resist protectionist pressures. Industrial countries should honour commitments to liberalise their agricultural trade.

Developing countries

6. For some heavily indebted low income countries, additional conditional loans from official sources on concessional terms are essential. Emphasise contribution that Chancellor's Sub-Sahara initiative could make.

7. Greater commitment to sound financial policies and structural reform among middle income debtors would help convince creditors that good money was not being thrown after bad. It would also help to stem capital flight. Debt relief for some countries could prejudice future financing.

8. Main contributions that industrial countries can make to alleviation of middle income debt problems are sustained economic growth, stable financial conditions, and liberalisation of trade restrictions (especially in agricultural products).

9. Currencies of some developing countries have become substantially under-valued. Taiwan and Korea, especially, should be encouraged to liberalise their trade. The efforts of these NICs to penetrate overseas markets, whilst maintaining barriers to protect their own domestic markets, are source of protectionist pressure in developed countries - particularly the United States.

BACKGROUND

Industrial countries

1. No major disagreements with IMF forecasts, which for output in the major seven in 1987 and 1988 are similar to the OECD's and to our own. Downward revisions to prospects for France and especially Germany in 1987 reflect disappointing performance over the year so far. Recent positive signs have led to upward revision to prospects for Japan. Agreement on moderate growth overall to end-1988 in industrial countries. Also agreement that underlying inflation in industrial countries will remain low. There are few signs of capacity constraints, except perhaps in US, where unemployment may be close to natural rate.

		IMF	OECD	June WEP
			Percentage changes	
Real GNP*	1987	2.5	2¼	2.4
	1988	2.7	2½	2.8
Consumer prices*	1987	2.9	3	2.6
	1988	3.4	3½	3.2
Volume of world trade	1987	3.6	2¼	2.8
	1988	4.5	4	4.2

* Major seven.

2. In the Louvre Agreement the United States said it would reduce the Federal deficit from an estimated 3.9 per cent of GNP in fiscal 1987 to 2.3 per cent (the Gramm-Rudman-Hollings target) in fiscal 1988. In the event, the deficit is likely to be a little lower than estimated for fiscal 1987 (at around 3.7 per cent), largely because of one-off receipts from tax reform. With existing tax rates and expenditure programmes, the Administration estimates that the deficit would decline only to 3.4 per cent in FY1988, and the IMF that it would remain unchanged at 3.7 per

cent. The present stalemate between the Administration and Congress on the Federal Budget for FY1988 gives little ground for hope that the deficit will be much below this.

3. The fiscal stance in Japan is hard to assess. A 'Y6 trillion' package, first announced in April, was presented in greater detail on 29 May. The 'Y6 trillion' includes sums made available for loans to private corporations for investment. Impact therefore depends on take up by private sector. The impact of the increase in disaster contingency fund of Y450 billion is also unclear, and about one-third of the package comprises spending by local authorities. However, IMF staff tentatively estimates that the package will raise Japanese GNP by ½ per cent this year and by 1 - 1½ per cent in 1988.

4. Soon after the Louvre Agreement, the German Government announced that income tax cuts of DM5.2 billion or 0.3 per cent of GNP (part of the larger tax reform originally scheduled for 1990) would be brought forward to next January. However, with public expenditure planned to continue to decline relative to GNP, the overall stance of fiscal policy in Germany is still not expansionary, in circumstances of low inflation and weak growth.

Developing countries

5. The experience of developing countries has been highly diverse over past two years. Oil producers and primary producers (many in Sub-Sahara) have suffered. But oil importers and manufacturers (particularly in Asia) have done well. Differences in performance have also reflected differences in domestic policies - successful domestic adjustment to adverse external developments of some countries which have avoided debt-servicing difficulties contrasting with lack of adjustment in countries with debt problems.

6. Commodity prices have recovered a little this year, and given sustained growth in industrial countries could strengthen further. This should help the position of many of the developing countries that have been hardest hit.

ds2

HER MAJESTY'S TREASURY

BRIEFING FOR THE 1987 ANNUAL MEETINGS OF THE IMF, IBRD AND COMMONWEALTH FINANCE MINISTERS

THE US ECONOMY

Economic Situation

1. Following an increase of little more than 2 per cent during 1986, real GNP rose at an annual rate of 3¼ per cent during the first half of 1987. The Administration believes that this rate of growth will be sustained through the year, but other forecasters are generally not so optimistic.

2. Employment has continued to grow rapidly and unemployment has continued to decline. At 6 per cent in July and August, the unemployment rate was at its lowest for seven and a half years.

3. In terms of the 12-month change in the total consumer price index, the inflation rate, which was down to only $^3/_4$ per cent at the end of last year, has risen sharply, to almost 4 per cent in July. However, as indicated by the index excluding food and energy, the underlying inflation rate has remained little changed, at around 4 per cent.

4. The trade deficit averaged $14.1 billion a month in the first half of the year - which, at about 4 per cent of GNP, is virtually unchanged from the average in 1986.

BASIC ECONOMIC STATISTICS

Percentage changes over year before	1984	1985	1986	1987 (Latest)
Real GNP	6.8	3.0	2.9	2.4 (Q2)
Nominal GNP	10.8	6.3	5.6	5.6 (Q2)
Consumer prices	4.3	3.5	1.9	3.9 (July)
Unemployment (per cent of labour force)	7.5	7.2	7.0	6.0 (Aug)
Industrial Production	11.5	1.7	1.0	3.2 (June)
Trade deficit ($bn)*	10.3	11.6	13.9	15.7 (June)

*Monthly average.

Budget Deficit

5. The Federal deficit, which reached $221 billion (5.3 per cent of GNP) in FY1986 (which ended last September), is expected to decline to about $160 billion (3.7 per cent) in FY1987. This decline reflects partly slower growth in defence expenditure but partly also transitory gains in revenue from an acceleration of payments of capital gains tax in anticipation of changes in the Tax Reform Act.

6. The Administration now forecasts a deficit for FY1988 of $123 billion (2.6 per cent of GNP), which is higher than the $102 billion originally stipulated by the Gramm-Rudman-Hollings Act. The Administration's forecast assumes that its expenditure proposals are enacted. It also assumes a growth rate of 3½ per cent. On current legislation and a lower growth rate of 2½ per cent a year, the Congressional Budget Office projects that the deficit would rise to $183 billion (about 4 per cent of GNP) in FY1988 and further to $192 billion (also about 4 per cent of GNP) in FY1989.

7. Congress is currently considering legislation to revise the Gramm-Rudman-Hollings deficit targets and re-establish automatic spending reduction procedures (the procedures in the original Act having been declared unconstitutional last year).

Financial Developments

8. After declining almost continuously for two and a half years, from a peak of around 11½ per cent in mid-1984 to below 6 per cent at the beginning of this year, 3-month rates have risen by about 1½ percentage points since January. Long-term rates have increased rather more, possibly reflecting heightened expectations of inflation.

9. In February M1 was dropped as a target aggregate, as its behaviour has been distorted by financial innovations. A range of 5½ - 8½ per cent for the growth rates of M2 and M3 has been retained. Growth rates of both of these broader aggregates have been running below the lower bound of the range this year, and M1 has also decelerated sharply. However, this has not caused the Fed to interpret monetary conditions as unduly tight.

Exchange Rate

10. From its peak in the first quarter of 1985 to the first quarter of 1987, the US dollar depreciated by 30 per cent in nominal effective terms, and by 38 per cent in real terms, as measured by relative unit labour costs in manufacturing. The dollar has been more stable since then, following the Louvre Agreement.

Monetary Indicators and the Dollar

	1985	1986	1987 Q1	Q2	Latest
3-month interest rates (%)	8.1	6.5	6.1	6.9	7.3 (8 Sept)
Long-term interest rates (%)	10.6	7.6	8.4	9.2	9.2 (31 Aug)
Money supply*:					
M1	12.5	16.5	15.5	11.9	10.1 (Aug)
M3	7.3	8.9	7.4	7.0	6.1 (July)
Effective dollar (1975=100)	140.7	114.8	104.6	101.0	100.2 (17 Sept)
Relative unit labour costs (1980=100)	146.5	112.5	99.0	-	-

* End of period; percentage changes on year before.

ECONOMIC OUTLOOK in EC
C

INFORMAL ECOFIN 11-13 SEPTEMBER 1987 **ANNEX C**

THE ECONOMIC OUTLOOK IN THE COMMUNITY

Attached are:

(1) a brief on the Commission's second quarterly review paper (Annex C1)

(2) the Commission's paper (Annex C2)

(3) economic statistics on the EC, US and Japan (Annex C3)

ECOFIN 11 - 13 SEPTEMBER ANNEX C1

ECONOMIC OUTLOOK IN THE COMMUNITY

Document: Second Quarterly Examination of the Economic Situation in the Community. – attached at Annex C2

UK Objectives

1. To avoid endorsing the Commission's plan for co-ordinated European reflation.

2. To record our views on the Commission's comments about UK policy.

Points to make

i. Gloomy tone of Commission's assessment exaggerated. Forecast slowdown in EC growth is slight - from 2½ per cent a year in 1985 and 1986 to 2¼ per cent in 1987. This is disappointing. It is not a recession. Governments should not be panicked into general expansionary fiscal measures.

ii. Commission's arguments in favour of concerted fiscal expansion overstated. Wishful thinking to suppose it could be largely self-financing, with faster growth generating extra revenues. But there may be scope in a few countries, e.g. Germany, for more flexible policy response.

see p 37 A C2

iii. Disagree most strongly with recommendations for UK budgetary policy. Domestic demand is currently very buoyant and output growth (4 per cent between 1986H1 - 1987H1) well above the growth of productive potential. Substantial further growth likely in 1988. Hardly the circumstances in which a demand stimulus is required.

C1

Background note

1. We have no major disagreements with the Commission's assessment of the economic situation and prospects in the Community. It may be a little pessimistic on growth, especially for 1988. The figures that have appeared recently, since the Commission's forecast was made in April/May, have been moderately encouraging. After a bad first quarter, where GNP fell in Germany and Italy and increased only fractionally in France, industrial production has picked up somewhat in these countries:

Index of Industrial Production (1980=100)

	Germany	**France**	**Italy**
1986Q4	107	102	99
1987Q1	105	101	102
April/May	108	103	104

Fears of a recession in Europe have receded. Nevertheless, the growth of the French and German economies is likely to remain disappointingly slow.

2. However, our latest assessment is that UK growth is likely to be higher than the 3.1 per cent predicted by the Commission for 1987, while the current account deficit may be lower.

3. The Commission calls for an easing in fiscal policy in countries with relatively low budget deficits. It argues that the main reasons why these countries are reluctant to run larger budget deficits are balance of payments constraints and/or revenue shortfalls due to slow growth. Thus the attraction of a concerted fiscal expansion (which it seems to believe could almost be self-financing).

4. The UK is identified as one of five countries with room for manoeuvre on fiscal policy. On page 37 it is argued that "in the context of joint Community action, there would be a case for allowing the PSBR in 1988-89 to rise above the level set for the medium-term". As was stressed at Budget time, the PSBR (excluding privatisation receipts) should decline gradually in the medium-term. It is government policy to set a steady path for the PSBR. And latest developments point to considerable buoyancy of the economy.

PREPARATION FOR IMF/IBRD

B

TO ALL MEMBERS OF THE MONETARY COMMITTEE

ANNEX B1

THERE FOLLOWS THE TEXT OF THE DRAFT STATEMENT TO BE MADE BY MR SIMONSEN TO THE INTERIM COMMITTEE OF THE IMF, INCORPORATING THE CHANGES MADE AT THE MEETING OF THE MONETARY COMMITTEE ON 2 SEPTEMBER.

A. KEES

9/9/87

B1

DRAFT STATEMENT BY MR PALLE SIMONSEN,
CHAIRMAN OF THE COUNCIL OF THE EUROPEAN COMMUNITIES,
TO THE IMF/IBRD ANNUAL MEETINGS OF SEPTEMBER 1987

1. SINCE DENMARK CURRENTLY HOLDS THE PRESIDENCY OF THE COUNCIL OF THE EUROPEAN COMMUNITIES, I HAVE THE HONOUR TO ADDRESS YOU IN THE NAME OF THE MEMBER STATES.

2. WORLD ECONOMIC DEVELOPMENTS OVER THE LAST 12 MONTHS HAVE NOT LIVED UP TO INITIAL FORECASTS. IN THE COURSE OF THE WINTER 1986/87 THERE WERE SIGNS OF WEAKENING IN DEMAND AND PRODUCTION IN SEVERAL INDUSTRIALIZED COUNTRIES. A CLEAR SENSE OF UNCERTAINTY WAS NOTICEABLE DURING THIS PERIOD, WHICH, IF SUSTAINED, WOULD LIKELY HAVE NEGATIVE EFFECTS ON THE WORLD ECONOMY.

HOWEVER, WE ARE CONFIDEMT THAT BOTH DEMAND AND PRODUCTION ARE NOW AGAIN ON AN UPWARD TREND. ALTHOUGH THE DECLINE IN ENERGY PRICES HAS BEEN PARTIALLY REVERSED IN 1987, WE THINK THAT PRICE DEVELOPMENTS SO FAR HAVE BEEN ENCOURAGING. NEVERTHELESS, IT IS WORRYING THAT, BOTH WITHIN THE EUROPEAN COMMUNITY AND IN MOST OTHER INDUSTRIALIZED COUNTRIES, WE ARE STILL FACED WITH A RATE OF UNEMPLOYMENT WHICH IS TOO HIGH, WITH A RATE OF NEW PRODUCTIVE INVESTMENT WHICH IS STILL INADEQUATE AND WITH LARGE CURRENT ACCOUNT IMBALANCES IN THE MAJOR INDUSTRIAL COUNTRIES, WHICH ARE, HOWEVER, DECLINING IN REAL TERMS.

3. AGAINST THE BACKGROUND OF THE VERY SUBSTANTIAL ADJUSTMENT OF EXCHANGE RATES WHICH TOOK PLACE IN 1985/86, THE AGREEMENT REACHED IN PARIS IN FEBRUARY, WHICH WAS SUBSEQUENTLY SUPPORTED BY THE APRIL MEETING OF THE INTERIM COMMITTEE OF THE IMF AND BY THE VENICE SUMMIT IN JUNE, PROVED TIMELY AND SUCCESSFUL. IT HAS CONTRIBUTED TO A BETTER FUNCTIONING OF THE INTERNATIONAL MONETARY SYSTEM, ESPECIALLY BECAUSE IT WAS BACKED UP BY DOMESTIC POLICY COMMITMENTS.

AS WAS STATED IN THE PARIS MEETING, A PRECONDITION FOR EXCHANGE RATE STABILITY AND MORE BALANCED GLOBAL GROWTH IS THAT THE POLICIES ANNOUNCED BY THE MAJOR COUNTRIES BE FULLY IMPLEMENTED AND THAT ECONOMIC POLICY COORDINATION BE INTENSIFIED. IN THIS CONTEXT WE WELCOME THE GREATER USE OP INDICATORS AS AN INSTRUMENT OF MULTILATERAL SURVEILLANCE TO PROMOTE INTERNATIONAL ECONOMIC POLICY COORDINATION.

4. IN PARALLEL WITH THE INTERNATIONAL EFFORTS TO ACHIEVE A HIGHER DEGREE OF EXCHANGE RATE STABILITY, AT THE EUROPEAN LEVEL WE ARE PROCEEDING IN OUR ENDEAVOURS TO STRENGTHEN MONETARY COOPERATION WITHIN THE EMS. WE FEEL THAT DEVELOPMENTS SINCE EARLY 1987 HAVE BEEN SATISFACTORY, AND WE ARE PRESENTLY SEEKING WAYS TO IMPROVE OUR COOPERATION IN THE MONETARY FIELD EVEN FURTHER. IN LINE WITH THE APPROACH FOLLOWED WITHIN THE IMF AND WITH THE DECLARATION ADOPTED AT THE WORLD ECONOMIC SUMMIT IN VENICE IN JUNE WE ALSO ARE PLANNING TO MAKE INCREASED USE OF INDICATORS IN OUR INTERNAL SURVEILLANCE ACTIVITIES AIMED AT IMPROVING THE CONVERGENCE OF ECONOMIC FUNDAMENTALS WITHIN THE COMMUNITY.

5. WE FIND DEVELOPMENTS SO FAR IN THE URUGUAY ROUND SATISFACTORY, BUT MUCH NEEDS TO BE DONE TO CONCLUDE THE PREPARATORY PHASE SUCCESSFULLY BY THE END OF THIS YEAR. THE EUROPEAN COMMUNITY INTENDS TO PARTICIPATE CONSTRUCTIVELY IN THESE NEGOTIATIONS. WE ARE VERY CONCERNED ABOUT THE PRESSURES FOR INCREASING PROTECTION WHILE THE TRADE NEGOTIATIONS ARE STILL IN PROGRESS. ONE PARTICULARLY DIFFICULT AND SENSITIVE SUBJECT IN THIS CONTEXT IS THE QUESTION OF INTERNATIONAL TRADE IN AGRICULTURAL PRODUCTS. ALMOST ALL COUNTRIES BEAR SOME RESPONSIBILITY FOR CURRENT PROBLEMS. WITHIN THE EUROPEAN COMMUNITY WE ARE AWARE OF OUR RESPONSIBILITIES IN THIS FIELD.

6. WE WELCOME THE SATISFACTORY CONCLUSIONS OF UNCTAD VII, WHICH HAVE LED TO A COMMON EVALUATION OF THE INTERNATIONAL ECONOMIC SITUATION AND TO A WILLINGNESS TO STRENGTHEN THE EFFORTS OF THE INTERNATIONAL COMMUNITY.

7. TURNING NOW TO THE DEBT STRATEGY, THE MEMBER STATES OF THE COMMUNITY REMAIN COMMITTED TO THE CASE-BY-CASE APPROACH WHICH ASSURES THE BEST POSSIBILITIES OF TAKING INTO ACCOUNT THE SPECIAL CIRCUMSTANCES OF DIFFERENT INDEBTED COUNTRIES. WHILE THIS STRATEGY HAS SERVED ALL THE PARTIES CONCERNED WELL, IT HAS ALSO FOR SOME TIME BEEN EVIDENT THAT IT NEEDS REINFORCEMENT AND THAT ALL ITS ELEMENTS HAVE TO BE IMPLEMENTED MORE EFFECTIVELY.

8. VIEWED AGAINST THIS BACKGROUND, SOME POSITIVE DEVELOPMENTS HAVE TAKEN PLACE SINCE THE MEETING OF THE INTERIM COMMITTEE IN APRIL THIS YEAR, IN PARTICULAR IN REGARD TO THE POOREST COUNTRIES, AND AMONG THESE PRIMARILY THE SUB-SAHARAN AFRICAN COUNTRIES, FOR WHICH THE OUTLOOK REMAINS BLEAK. INTENSIFIED DELIBERATIONS IN THE PARIS CLUB HAVE ALREADY RESULTED IN LONGER REPAYMENT AND GRACE PERIODS WITH RESPECT TO RESCHEDULED OFFICIAL CREDITS FOR CERTAIN COUNTRIES IN SUPPORT OF THEIR FAR-REACHING ECONOMIC REFORMS. PROPOSALS FOR LOWER INTEREST RATES HAVE BEEN PUT FORWARD.

too much prominence to Camdessus?

AN IMPORTANT NEW DEVELOPMENT IS THE PROPOSAL BY THE MANAGING DIRECTOR OF THE IMF FOR A SUBSTANTIAL INCREASE IN THE RESOURCES OF THE FUND'S STRUCTURAL ADJUSTMENT FACILITY (SAF) OVER THE THREE-YEAR PERIOD 1988-90, TO BE ASSOCIATED WITH THE ADOPTION OF STRONG GROWTH-ORIENTED ADJUSTMENT PROGRAMS BY LOW-INCOME COUNTRIES IN CLOSE COLLABORATION WITH THE WORLD BANK.

THE MEMBER STATES OF THE COMMUNITY WELCOME THE PRINCIPLES UNDERLYING THESE PROPOSALS AND, DESPITE SOME DIFFICULT ISSUES WHICH ARE NOT ALL PURELY TECHNICAL, SHARE THE WILLINGNESS TO CONCLUDE DISCUSSIONS ON THESE PROPOSALS BY THE END OF THIS YEAR. IN THE CONTEXT OF THIS FACILITY, COLLABORATION BETWEEN THE IMF AND THE WORLD BANK WILL BE IMPORTANT FOR THE ENVISAGED CATALYTIC ROLE OF THE FACILITY TO MATERIALIZE.

PRIMARY PRODUCT EXPORTERS, AND PARTICULARLY THOSE DEPENDENT ON A SINGLE COMMODITY, DESERVE SPECIAL CONSIDERATION AND IT MAY BE APPROPRIATE TO MAKE ADEQUATE RESOURCES AVAILABLE TO THEM ON CONCESSIONAL TERMS. ?

9. AS FAR AS THE MIDDLE-INCOME DEBTORS ARE CONCERNED THERE HAVE BEEN FURTHER USEFUL INNOVATIONS BROADENING THE RANGE OF PROCEDURES AND FINANCING TECHNIQUES BY COMMERCIAL BANK CREDITORS WHICH HOPEFULLY WILL FACILITATE THE ASSEMBLING AND IMPLEMENTATION OF FINANCIAL PACKAGES. HOWEVER, THE PROCESS OF NORMALIZING DEBTOR/CREDITOR RELATIONS SO AS TO REGAIN NORMAL MARKET ACCESS IS INEVIABLY TAKING A LONG TIME. ALTHOUGH PROGRESS HAS BEEN MADE IN SEVERAL COUNTRIES, IN SOME DEBTOR COUNTRIES THE PERSEVERANCE IN ADJUSTMENT POLICIES HAS NOT ALWAYS MEASURED UP TO WHAT IS NEEDED, AND FINANCING FLOWS TO THE DEVELOPING COUNTRIES HAVE FALLEN SHORT OF EXPECTATIONS.

ALL PARTIES INVOLVED MUST MAKE FURTHER PROGRESS IN A COOPERATIVE SPIRIT FOR THE FULL IMPLEMENTATION OF THE DEBT STRATEGY, WITH THE VITAL SUPPORT OF PRIVATE FINANCING, BOTH BY THE BANKS AND IN THE FORM OF NON-DEBT CREATING CAPITAL FLOWS TO DEBTOR COUNTRIES.

10. THE MEMBER STATES OF THE COMMUNITY CONTINUE TO TAKE THE VIEW THAT THE RESOURCES OF THE IMF SHOULD PREDOMINANTLY COME FROM QUOTA SUBSCRIPTIONS. FOR THE IMF TO BE ABLE TO CONTINUE TO PLAY A CENTRAL ROLE BOTH IN THE ADJUSTMENT PROCESS AND AS THE GLOBAL MONETARY INSTITUTION IT WILL BE IMPORTANT THAT THE FUND HAS SUFFICIENT USABLE RESOURCES. THEREFORE, WE WELCOME THAT THE EXECUTIVE BOARD HAS INITIATED DISCUSSIONS ON THE NINTH GENERAL REVIEW OF QUOTAS, IN WHICH THE MEMBER STATES OF THE EC WILL PARTICIPATE CONSTRUCTIVELY.

11. THE MEMBER STATES OF THE COMMUNITY ADHERE TO THE VIEW THAT THE FUND'S ENLARGED ACCESS POLICY IS A TEMPORARY FACILITY. HOWEVER, IN VIEW OF THE CONTINUED PAYMENTS IMBALANCES AND DIFFICULTIES IN SEVERAL MEMBER COUNTRIES WE ARE PREPARED TO SUPPORT A CONTINUATION OF THAT POLICY FOR 1988.

THE MEMBER STATES OF THE EUROPEAN COMMUNITY ALSO LOOK FORWARD TO THE RESULTS OF THE ONGOING REVIEW OF THE COMPENSATORY FINANCING FACILITY.

12. OVER THE PAST COUPLE OF YEARS THERE HAS BEEN AN INCREASING COOPERATION BETWEEN THE IMF AND THE WORLD BANK IN PARTICULAR WITH RESPECT TO THE POOREST DEVELOPING COUNTRIES IN SOLVING THEIR ECONOMIC PROBLEMS.

A SITUATION WHERE THE NEEDS OF THE DEVELOPING COUNTRIES ARE INCREASING RATHER THAN DECREASING AND WHERE WORLD BANK LENDING IS APPROACHING THE STATUTORY LIMITS, UMDERLINES THE NEED FOR AN EARLY AGREEMENT ON A GENERAL CAPITAL INCREASE.

13. AN IMPORTANT CONTRIBUTION TO EASING THE PROBLEMS OF THE POOREST COUNTRIES SHOULD ALSO COME FROM THE HIGH LEVEL REACHED FOR IDA 8. WE THEREFORE HOPE THAT IT WILL BE POSSIBLE FOR DONOR GOVERNMENTS TO COMPLETE RAPIDLY THEIR DOMESTIC PROCEDURES TO ENSURE A TIMELY IMPLEMENTATION OF THE REPLENISHMENT.

14. THE MEMBER STATES OF THE EUROPEAN COMMUNITY FEEL STRONGLY THAT SPECIAL AND INNOVATIVE MEASURES ARE CALLED FOR TO HELP DEBT-DISTRESSED COUNTRIES IN SUB-SAHARAN AFRICA UNDERTAKING RIGOROUS POLICY REFORM. THE WORLD BANK TOGETHER WITH THE IMF HAS AN ESSENTIAL ROLE TO PLAY IN PROMOTING AND COORDINATING THESE MEASURES. WE THEREFORE WELCOME THE INCREASED EMPHASIS ON THESE ISSUES AS RECENTLY REFLECTED IN THE BANK'S PROPOSAL FOR A SPECIAL ACTION PROGRAM AIMED AT A CONCERTED EFFORT FOR ADDITIONAL FINANCING FROM THE DONOR COMMUNITY IN ORDER TO ASSIST THE SUB-SAHARAN COUNTRIES' OWN EFFORTS IN TACKLING THEIR PROBLEMS.

15. THE EC-COUNTRIES HOPE THAT THE REQUISITE NUMBER OF RATIFICATION INSTRUMENTS WILL BE DEPOSITED SOON TO ALLOW MIGA TO ENTER INTO FORCE. WE ARE CONVINCED THAT THIS NEW ARRANGEMENT WILL PLAY A BENEFICIAL ROLE IN PROMOTING AND SUPPORTING FOREIGN DIRECT INVESTMENT.

NNNN

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End of message

COVERING CONFIDENTIAL

FROM: JANET BARBER
DATE: 9 SEPTEMBER 1987

CHANCELLOR

INFORMAL ECOFIN 11-13 SEPTEMBER

You are attending the informal ECOFIN in Nyborg in Denmark this weekend. Sir Geoffrey Littler and Mr Leigh Pemberton will also be there.

2. The meeting itself is on Saturday 12 September. The Danes have circulated the following agenda:

<u>Morning</u>

(a) strengthening of the EMS and liberalisation of capital movements.

<u>Afternoon</u>

(b) preparation for the annual meetings of the IMF and IBRD, including the Presidency speech, the international economic situation and the proposed increase in the resources of the IMF's Structural Adjustment Facility.

3. Following discussion at the July ECOFIN lunch, the following might also be raised in the meeting:

(c) the economic outlook in the Community;
(d) the 1988 Community budget and reference framework.

Following discussion in the Monetary Committee in July, there may be a report on:

(e) the economic situation in Greece.

In addition, you may wish to raise the following in the margins of the meeting:

(f) with Herr Stoltenberg, capital convergence.*

M Balladur may expect to discuss with you:

(g) the Economic Policy Report on the CAP;

And others may raise:

(h) tax approximation;
(i) future financing of the Community;
(j) Council discussion on insurance (and possibly other financial services) under the Danish presidency;
(k) the proposed Belgian toll on foreign cars.

* Miss Noble is preparing a letter for you to hand over to Stoltenberg.

See separate [illegible] note
you have this separately

EMS AND CAPITAL MOVEMENTS

4. Mr Peretz will submit briefing separately on this*, taking account of Sir Geoffrey Littler's discussion this week with the French.

5. The relevant texts are:

(1) report from the chairman of the Monetary Committee;
(2) report from the Committee of Central Bank Governors;
(3) a Commission paper circulated by the Presidency - "The complete liberalisation of capital movements and strengthening the EMS". — now attached to Peretz note

A draft of (1), and copies of (2) and (3) are attached at **Annexes A1, A2, and A3** respectively.

6. The two reports address themselves to the remit given to the Committees following the January 1987 EMS realignment ie that they should examine measures to improve the operating mechanisms of the EMS. ECOFIN was given interim reports in April and June, and these are the final reports.

7. The Commission paper sets out its ideas on EMS development. It also describes the legislative proposals for full liberalisation of capital movements which the Commission plans to submit to the Council this autumn.

PREPARATION FOR THE IMF/IBRD ANNUAL MEETINGS

8. ECOFIN will as usual be asked to clear the EC Presidency speech to the IMF Interim Committee. This has been agreed in the Monetary Committee, and we have no problems with it. A copy is attached at **Annex B1.** However we understand that some points may be raised at the meeting:

(a) the reference to protectionism in paragraph 5 may be directed more explicitly towards the US if Congress passes any protectionist legislation this month;
(b) a reference to unchanged access limits for 1988 might be added to the second sentence of paragraph 11 if a common position on this is reached. We would support this addition.
(c) it may be explained that no reference to SDR allocation has been made because of the lack of a common position. We do not want an SDR allocation, but in the absence of agreement on this, are content with no reference to it in the speech;
(d) Delors may want some reference to the Commission's proposal on Community aid to sub-Saharan Africa. (This should be resisted - see paragraph 10 below).

9. The main items for discussion under this agenda item are likely to be sub-Saharan debt and the proposed increase in the IMF's Structural Adjustment Facility. A brief on this prepared by Mr Mountfield is at **Annex B2.** However, Sir Geoffrey Littler may wish to supplement this when he returns from Paris. The Commission paper on sub-Saharan debt which has been circulated by the Presidency is attached to Annex B2.

* Now enclosed below, covering Annex A1, A2, A3.

10. The Commission paper suggests inter alia action at Community level viz a 100 mecu Community programme financed in effect from the European Development Fund (whose resources are provided by member states outside the Community budget) and speeding up of Lome III payments. Details of this proposal have not yet been made available to member states, and we should avoid commitment to any of them at this ECOFIN.

11. There will also be some discussion on the world economic outlook. IF division's **draft** brief on this topic for the Annual Meetings is attached at **Annex B3.** Please see also the briefing material for the economic outlook in the Community (Annex C).

12. There may be some discussion on G10 issues - if so Sir Geoffrey Littler will brief you direct. (papers in front flap)

THE ECONOMIC OUTLOOK IN THE COMMUNITY

13. This is covered in **Annex C.**

14. At its July meeting, ECOFIN conducted the second quarterly review of the economic situation in the Community, on the basis of a Commission paper. It was agreed that the policy guidelines in the 1986-87 Annual Economic Report need not be changed. However the Danish Presidency concluded that the economic situation should be carefully monitored and reconsidered at this informal ECOFIN. Annex C includes:

(1) a brief on the Commission's second quarterly review paper - you may recall that this suggested that the UK should allow the PSBR to rise (Annex C1);
(2) a copy of the Commission's paper (Annex C2);
(3) the usual economic statistics on the EC, US and Japan (Annex C3).

The latest information from the Presidency is that this will probably not be raised as a separate item, but the briefing, particularly (3), can be drawn on for discussion of the world economic situation under the item on preparation for the Annual Meetings.

THE 1988 COMMUNITY BUDGET AND REFERENCE FRAMEWORK

15. This is covered in **Annex D.**

16. At the July ECOFIN lunch, Commissioner Christophersen asked how the Budget Council could sensibly approach setting a budget for 1988 constrained by the Council's unrealistic reference framework for agricultural market support. It was agreed that the informal ECOFIN might discuss the matter further. As the July Budget Council failed to agree on a draft budget for 1988, the point remains unresolved.

17. The latest information from the Presidency is that this will not be raised, and Commissioner Christophersen will not be present, at the informal ECOFIN. Therefore the briefing at Annex D is provided on a contingent basis.

THE ECONOMIC SITUATION IN GREECE

18. This is covered in **Annex E.**

19. In November 1985, ECOFIN agreed on a 1.75 billion ecu loan to Greece under the Community Loan Mechanism to help with balance of payments problems. The loan was in two equal tranches, the first being authorised in November 1985 and the second in December 1986. The loan package also included economic recovery targets for 1986 and 1987, and authorisation for some capital movements restrictions (until November 1988), import deposits (ended in April this year), and export subsidies (due to be phased out by the beginning of 1990). The CLM loan Decision provided that the Monetary Committee would periodically examine the Greek economic recovery programme against the targets set.

20. The Monetary Committee last examined the Greek economy in July. The Committee expressed concern that some of the recovery targets for 1987, especially that for inflation, would not be met, and felt that there was a clear need for the stabilisation programme to be continued into 1988. In line with normal procedure, the Chairman (Tietmeyer) said that he would write to Mr Simitis. He said also that he would report orally to the informal ECOFIN at lunch. There was, however, no indication that there would be any substantive discussion, and latest contacts with the Presidency confirm that discussion is unlikely. Therefore Annex E gives background briefing only.

CAPITAL CONVERGENCE

21. It is suggested that you raise this with Herr Stoltenberg, with the aim of obtaining German support for the current drive on capital adequacy ~~conversion~~. convergence.

22. The arguments and line to take are set out in Miss Noble's submission of today,* and a copy of her aide memoire is attached at **Annex F.**

THE ECONOMIC POLICY COMMITTEE REPORT ON THE CAP

23. This is covered in **Annex G.** M Balladur might be expecting to discuss it with you.

24. The Economic Policy Committee (EPC) has recently been considering the Community's agricultural policy, and its French chairman, M Milleron has now produced a report (copy attached to Annex G). M Balladur is aware that we have in mind a possible ECOFIN discussion of it at some stage, and he may mention this to you. It is suggested that you explore M Balladur's views on the handling of the report.

TAX APPROXIMATION

25. We know that the Danish Presidency does not wish to raise tax approximation, and believe that the Commission are unlikely to do so (Lord Cockfield will not be present). However in case others

* Enclosed below covering Annex F

mention it in the meeting itself or in the margins, **Annex H** gives a line to take.

FUTURE FINANCING OF THE COMMUNITY

26. Again this is not on the agenda, but in case it is raised **Annex I** gives a summary of the present position and the likely timetable for negotiations for the remainder of the year.

27. In particular, Herr Stoltenberg may be concerned about possible costs to Germany, including the cost of the UK refund. If he mentions this, you could remind him that the UK is still the second largest net contributor to the Community budget, and that we are looking to improve or at least maintain our refund arrangements under any new financing system.

COUNCIL DISCUSSION ON INSURANCE UNDER THE DANISH PRESIDENCY

28. This is unlikely to be raised. However it is just possible that some member states may be concerned about the Danes' apparent plans to take Council discussion of insurance (and perhaps some other financial services) in the Internal Market Council (IMC) rather than in ECOFIN during their Presidency.

29. You may recall that DTI consulted us about this in preparation for the informal IMC on 7 September, and the issues were set out in my submission of 1 September (reproduced at **Annex J**, together with Ms Ryding's minute of 2 September). In fact the matter was not raised at the IMC, the Presidency merely stating, in the general context of arrangements for Councils, that they would do what seemed best at the time.

30. In case the matter is mentioned you might like to be reminded of the line we took with DTI:

(a) on **insurance**, we would not stand in the way of the transfer subject to the caveat that all other member states were happy.
(b) on **other financial services**, we would not want to see a transfer from ECOFIN to the IMC without discussion in Coreper of the particular circumstances involved, and that in particular we would have a very strong presumption against the transfer of banking and mortgage credit items.

THE PROPOSED BELGIAN TOLL ON FOREIGN CARS

31. The Belgians have said recently that they intend to introduce a tax on foreign vehicles using Belgian motorways. Other member states, especially the Germans and Dutch, are opposed to this, and may mention it at ECOFIN. In case they do **Annex K** gives a line to take.

PERSONALITY NOTES

32. The usual notes are attached - top copy only. This will be the first ECOFIN for the new Italian Treasury minister, Giuliano

Amato.

33. Copies of this briefing go to those on the attached list.

Janet Barber

JANET BARBER
EC1

CIRCULATION

PS/Chancellor
Sir Geoffrey Littler
Mr Lavelle
Mr Edwards
Mr C Budd, Cabinet Office
Mr J S Wall, FCO
The Governor B/E
Mr D Bostock, UKREP (2 copies)

Steering brief only

PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Sir Peter Middleton
Mr Byatt
Mr P Cropper
Mr Scholar
Mr Peretz
Mr Mountfield
Mr Culpin
Mr Ilett
Mr Matthews
Mr Crabbie
Mr Mortimer
Mr Kelly
Miss Noble
Ms Sinclair
Mrs Imber
Mr Batt
Mr Savage
Mr Williams
Mr J Kirby B/E
Mr Garside - Paris
Mr A C Thorpe - Bonn
Mr T P Lankester - Washington
Miss C Elmes - Rome
Ms French C&E
Mr Oxenford C&E
Mr Crooke DTP.

INFORMAL ECOFIN 11-13 SEPTEMBER 1987 **ANNEX B**

PREPARATION FOR THE IMF/IBRD ANNUAL MEETINGS

Attached are:

(1) the EC Presidency speech to the IMF Interim Committee

(2) Mr Mountfield's brief on sub-Saharan debt and the Structural Adjustment Facility, with two attachments:

(i) the Commission paper on sub-Saharan debt circulated by the Presidency
(ii) the UK Memorandum on sub-Saharan debt

(3) IF's draft brief for the IMF/IBRD Annual meetings on the world economic outlook

3763/058

SECRET

PWP

FROM: P D P BARNES
DATE: 10 September 1987

MR PERETZ

cc PS/Chancellor
Sir P Middleton
Sir G Littler
Mr Cassell
Mr Lavelle
Mr H P Evans
Mr C W Kelly
Miss Barber
Ms Goodman

INFORMAL ECOFIN: STRENGTHENING THE EMS AND LIBERALISATION OF CAPITAL MOVEMENTS

The Economic Secretary has seen your submission to the Chancellor of 9 September.

2. The Economic Secretary would be grateful to know what are the main points of the 1972 Directive and why (apart from the obligation to retain exchange controls) we object to them.

PB

P D P BARNES
Private Secretary

SECRET

Pup

CONFIDENTIAL

ACSA
To see. (No need to show Ch, I think).
25 14/9

From: Sir G.Littler
Date: 14 September 1987

MR PERETZ

c.c. Mr Alex Allan
Sir P.Middleton
Mr Huw Evans
Mr Mountfield
Mr Kelly

INFORMAL ECOFIN

I thought that you and others might like advance sight of this reporting telegram. The meetings went harmoniously and on the whole satisfactorily, and were so reported in the press.

2. I shall be sending separately one or two notes on points which came up in the margins.

(Geoffrey Littler)

c.c. also:

Governor, B/E
Mr Loehnis, B/E

INFORMAL MEETING OF EC FINANCE MINISTERS AND GOVERNORS

Finance Ministers and Central Bank Governors of the Community met in Nyborg, Denmark, on 12 September. President Delors attended. The UK was represented by the Chancellor, the Governor and Littler (HMT). The plenary meeting ran from 9.15 a.m. until 3.45 p.m.

<u>Summary</u>

2. The meeting warmly endorsed some technical improvements in the operation of the Exchange Rate Mechanism to be implemented by the Committee of Central Bank Governors and the Monetary Committee. The Commission undertook to submit new Directives on liberalisation of capital movements and related matters, taking account of the discussion, for consideration by the Monetary Committee at its late October meeting and by ECOFIN in November. A Presidency statement for the annual IMF/IBRD meetings later this month in Washington was agreed. It was also noted that Lord Cockfield would present Commission proposals on tax approximation at the October ECOFIN: it was agreed that these would be remitted without discussion for consideration by the Economic Policy Committee and that Ministers would hold a restricted session on the subject before their December meeting (Ministers only).

<u>Strengthening the EMS</u>

3. Reports were presented from the Monetary Committee and the Committee of Central Bank Governors. Both were on similar lines. They emphasised the basic need for sound and compatible policies and proposed more systematic monitoring arrangements. They urged (and the Central Bank Governors reported that they had agreed on) some important technical improvements in the operation of the Exchange Rate Mechanism: extension of renewal arrangements for

Very Short-Term Financing; availability of such financing for intra-marginal intervention; extension of acceptability of ECU in settlements); they noted with regret the continuation of certain special regimes (Belgian two-tier exchange rate; Italian wider margins; absence of some countries from the ERM, and some also from the EMS) and they suggested that these special regimes should be kept under review; they urged liberalisation of capital movements.

4. President Delors welcomed both reports. He then outlined the proposals the Commission were preparing for new directives to embody the requirement of free capital movements, to revise the 1972 Directive on the subject, and to revise/amalgamate existing medium-term credit mechanisms.

5. In a lengthy discussion, in which all Ministers took part, the two reports were very warmly welcomed, and it was agreed to endorse the specific proposals for action made and agreed in them. Underlying what was actually said openly at the meeting was a sense of satisfaction that the previously rigid attitude of the Bundesbank on certain points had on this occasion been rather more flexible, enabling welcome progress to be made. Several Ministers indicated that the progress was greater than they had expected. Balladur (France) welcomed the reports in this spirit, but added that he would hope in due course for more diversification of EC members' official reserve holdings. The Chancellor took the same view.

Liberalisation of Capital Movements

6. President Delors outlined considerations which pre-occupied the Commission in drawing up directives on this subject, on which they insisted that more rapid and complete progress was needed as

part of the completion of the internal market. He focussed on the possible problems of discrepancies and distortions between national regimes of financial rules and supervision, of taxation and of rights of establishment; and on transitional arrangements for weaker countries and the need for safeguard clauses. He made a reference (picked up subsequently only by the Irish Minister) to the absence of sterling from the ERM and the risk that this might involve distortion and unfair competition.

7. The pressure by the Commission for liberalisation was generally accepted, indeed welcomed by a majority including the Chancellor. On the question whether there was a prior need for further progress in harmonisation of standards and supervision in banking and finance, in rights of establishment and in some areas of tax approximation, the Chancellor and others spoke strongly against, while fully endorsing the desirability of encouraging parallel action to remove impediments to free capital flow apart from exchange controls. The only residual worry was that of Danish Ministers, concerning the risk of loss of domestic tax revenues as a result of export of capital outside the domestic jurisdiction and system of reporting of income. From experience the Chancellor and others argued that lack of exchange control was not a decisive factor in such revenue loss, and that compensating Community-wide reporting systems, etc, would not solve the problem of tax havens outside the Community. Poos (Luxembourg) spoke very strongly on the theme that liberalisation was the key, that we should avoid comprehensive harmonisation which was a recipe for interminable argument, and avoid the associated bureaucracy.

8. There were wider differences of reactions to the concept of

safeguard clauses, including a Commission proposal to extend what they are advised is the legal coverage of present arrangements, but no attempt was made to press the debate.

9. There were some important comments on the 1972 Directive from Stoltenberg (no need to retain it), Ruding (it should be abolished because it is a wrong track from which we should now turn back), and the Chancellor (out of date; we could check if any of it was still relevant and incorporate such elements only in the proposed new directive).

10. Delors gave his own conclusions: that liberalisation should be implemented as soon as possible and need not await tax and other harmonisation; that the 1972 Directive was out of date, although it remained in his view an open question whether the Community needed a capacity for collective reaction to external pressures either way; that tax questions would need to be pursued because of the existing wide discrepancies which could become more damaging in a context of no exchange controls; and that the financial support mechanisms should be revamped, perhaps with some arrangement to use them positively to foster liberalisation.

11. A very poor initial summary by Simonsen was corrected and both his and Delors' press conference statements later in the day were a reasonably fair reflection of the discussion. Two features of the poor summary were egregious references to realignments and an enthusiastic demand for further study of the use of the ecu. Over lunch it was agreed to drop both.

Preparation of Washington Meetings

12. The draft Presidency statement was broadly agreed, although

some further changes may be proposed by the Presidency nearer the time. The discussion focussed on debt of the poorest countries. The Chancellor placed his own Sub-Sahara proposals and the IMF proposals for enlargement of the Structural Adjustment Facility in the same strategy and suggested both be pursued. He welcomed the similar view expressed in a Commission paper. Others who spoke favoured the IMF proposals, although several problems were mentioned. Only Amato (Italy) gave full support to the interest rate abatement proposal by the Chancellor, but others agreed that there should be further discussion in the Paris Club.

Tax Approximation

13. Over a separate lunch for Ministers only the conclusions of the morning meeting were settled and also the procedure for handling tax approximation as described in the summary.

1. T [illegible]
2 [illegible] (Washington)

CONFIDENTIAL

14/9/87.

Note for the Record

BILATERAL: CHANCELLOR/BALLADUR

In the margins of the informal ECOFIN in Nyborg on 11 September the Chancellor had a long bilateral talk with M. Balladur, French Finance Minister, accompanied by Trichet and Littler.

E.M.S.

2. Balladur judged that the Bundesbank had given rather more ground than expected, so that the outcome of the recent meeting of EC Central Bank Governors was quite good, even if less than he wanted. He would accept the conclusions reached on financing of intra-marginal intervention. He agreed with the Chancellor that ideas of 'diversification' of official reserves would be better pursued in the G5 than the EMS for the present.

3. His problem now was, he said, that the small remaining move France could take to remove their last exchange controls was the only card he had left in negotiations to get the Bundesbank to behave more cooperatively. He now had to decide whether to give it up. He suggested that the UK's great card was a much more potent one; but the Chancellor countered that it was not really a card suitable for negotiation, being altogether incommensurate. (Subsequently at the plenary meeting Balladur was delphic about his decision, seeming to leave it over until at least the next ECOFIN meeting. There must be an element of shadow-boxing here: Balladur must know that his 'card' does not greatly interest the Bundesbank).

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Poorest Debtors

4. After brief discussion it was agreed that the Chancellor's initiative should continue to be pursued in the Paris Club and the SAF in IMF fora. The Chancellor emphasised that they were both addressed to the same problem and should fit together. Balladur could not be persuaded to give support to the Chancellor, but he agreed that his initiative should be kept alive. (His attitude suggested that he would like the Chancellor to drop his idea, but could not afford politically to be seen to oppose it).

Other Matters

5. Three other points were mentioned by the Chancellor:

- EC Budget Figures: Balladur promised to study the figures Littler had given to Trichet, evidently not now wanting seriously to challenge our budget calculations.
- Milleron Report on Agriculture: Balladur professed to know nothing of this (to Trichet's embarrassment) but said he would now read it and consider what to do.
- G10 Membership: The Chancellor explained his proposal to admit Spain and Australia, then call a halt on what would be a defensible dividing-line; Balladur responded that this seemed sensible and brushed aside Trichet's attempt to remind him of what had obviously been rather different briefing by officials!

(Geoffrey Littler)

cc Mr. Alex Allan
Mr. Lavelle
Mr. Mountfield
Mr. H. Evans
Mr. Peretz
Mr. A.J.C. Edwards

FOR INTRA-MARGINAL INTERVENTION: EXTENSION OF ACCEPTABILITY OF ECU IN SETTLEMENTS): THEY NOTED WITH REGRET THE CONTINUATION OF CERTAIN SPECIAL REGIMES (BELGIAN TWO-TIER EXCHANGE RATE: ITALIAN WIDER MARGINS: ABSENCE OF SOME COUNTRIES FROM THE ERM, AND SOME ALSO FROM THE EMS) AND THEY SUGGESTED THAT THESE SPECIAL REGIMES SHOULD BE KEPT UNDER REVIEW: THEY URGED LIBERALISATION OF CAPITAL MOVEMENTS.

4. PRESIDENT DELORS WELCOMED BOTH REPORTS. HE THEN OUTLINED THE PROPOSALS THE COMMISSION WERE PREPARING FOR NEW DIRECTIVES TO EMBODY THE REQUIREMENT OF FREE CAPITAL MOVEMENTS, TO REVISE THE 1972 DIRECTIVE ON THE SUBJECT, AND TO REVISE/AMALGAMATE EXISTING MEDIUM-TERM CREDIT MECHANISMS.

5. IN A LENGTHY DISCUSSION, IN WHICH ALL MINISTERS TOOK PART, THE TWO REPORTS WERE VERY WARMLY WELCOMED, AND IT WAS AGREED TO ENDORSE THE SPECIFIC PROPOSALS FOR ACTION MADE AND AGREED IN THEM. UNDERLYING WHAT WAS ACTUALLY SAID OPENLY AT THE MEETING WAS A SENSE OF SATISFACTION THAT THE PREVIOUSLY RIGID ATTITUDE OF THE BUNDESBANK ON CERTAIN POINTS HAD ON THIS OCCASION HAD BEEN RATHER MORE FLEXIBLE, ENABLING WELCOME PROGRESS TO BE MADE. SEVERAL MINISTERS INDICATED THAT THE PROGRESS WAS GREATER THAN THEY HAD EXPECTED. BALLADUR (FRANCE) WELCOMED THE REPORTS IN THIS SPIRIT, BUT ADDED THAT HE WOULD HOPE IN DUE COURSE FOR MORE DIVERSIFICATION OF EC MEMBERS' OFFICIAL RESERVE HOLDINGS. THE CHANCELLOR TOOK THE SAME VIEW.

LIBERALISATION OF CAPITAL MOVEMENTS

6. PRESIDENT DELORS OUTLINED CONSIDERATIONS WHICH PRE-OCCUPIED THE COMMISSION IN DRAWING UP DIRECTIVES ON THIS SUBJECT, ON WHICH THEY INSISTED THAT MORE RAPID AND COMPLETE PROGRESS WAS NEEDED AS PART OF THE COMPLETION OF THE INTERNAL MARKET. HE FOCUSSED ON THE POSSIBLE PROBLEMS OF DISCREPANCIES OF DISTORTIONS BETWEEN NATIONAL REGIMES OF FINANCIAL RULES AND SUPERVISION, OF TAXATION AND OF RIGHTS OF ESTABLISHMENT: AND ON TRANSITIONAL ARRANGEMENTS FOR WEAKER COUNTRIES AND THE NEED FOR SAFEGUARD CLAUSES. HE MADE A REFERENCE (PICKED UP SUBSEQUENTLY ONLY BY THE IRISH MINISTER) TO THE ABSENCE OF STERLING FROM THE ERM AND THE RISK THAT THIS MIGHT INVOLVE DISTORTION AND UNFAIR COMPETITION.

7. THE PRESSURE BY THE COMMISSION FOR LIBERALISATION WAS GENERALLY ACCEPTED, INDEED WELCOMED BY A MAJORITY INCLUDING THE CHANCELLOR. ON THE QUESTION WHETHER THERE

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TO IMMEDIATE UKREP BRUSSELS
TELNO 333
OF 141800Z SEPTEMBER 87
AND TO IMMEDIATE ATHENS, BONN, BRUSSELS, COPENHAGEN, DUBLIN
AND TO IMMEDIATE THE HAGUE, LISBON, LUXEMBOURG, MADRID, PARIS, ROME
AND TO IMMEDIATE UKDEL IMF/IBRD WASHINGTON

BMP

INFORMAL ECOFIN, 12 SEPTEMBER
INFORMAL MEETING OF EC FINANCE MINISTERS AND GOVERNORS
FINANCE MINISTERS AND CENTRAL BANK GOVERNORS OF THE COMMUNITY MET IN NYBORG, DENMARK, ON 12 SEPTEMBER. PRESIDENT DELORS ATTENDED. THE UK WAS REPRESENTED BY THE CHANCELLOR, THE GOVERNOR AND LITTLER (HMT). THE PLENARY MEETING RAN FROM 9.15 AM UNTIL 3.45 PM.
SUMMARY
2. THE MEETING WARMLY ENDORSED SOME TECHNICAL IMPROVEMENTS IN THE OPERATION OF THE EXCHANGE RATE MECHANISM TO BE IMPLEMENTED BY THE COMMITTEE OF CENTRAL BANK GOVERNORS AND THE MONETARY COMMITTEE. THE COMMISSION UNDERTOOK TO SUBMIT NEW DIRECTIVES ON LIBERALISATION OF CAPITAL MOVEMENTS AND RELATED MATTERS, TAKING ACCOUNT OF THE DISCUSSION, FOR CONSIDERATION BY THE MONETARY COMMITTEE AT ITS LATE OCTOBER MEETING AND BY ECOFIN IN NOVEMBER. A PRESIDENCY STATEMENT FOR THE ANNUAL IMF/IBRD MEETINGS LATER THIS MONTH IN WASHINGTON WAS AGREED. IT WAS ALSO NOTED THAT LORD COCKFIELD WOULD PRESENT COMMISSION PROPOSALS ON TAX APPROXIMATION AT THE OCTOBE ECOFIN: IT WAS AGREED THAT THESE WOULD BE REMITTED WITHOUT DISCUSSION FOR CONSIDERATION BY THE ECONOMIC POLICY COMMITTEE AND THAT MINISTERS WOULD HOLD A RESTRICTED SESSION ON THE SUBJECT BEFORE THEIR DECEMBER MEETING (MINISTERS ONLY).
STRENGTHENING THE EMS
3. REPORTS WERE PRESENTED FROM THE MONETARY COMMITTEE AND THE COMMITTEE OF CENTRAL BANK GOVERNORS. BOTH WERE ON SIMILAR LINES. THEY EMPHASISED THE BASIC NEED FOR SOUND AND COMPATIBLE POLICIES AND PROPOSED MORE SYSTEMATIC MONITORING ARRANGEMENTS. THEY URGED (AND THE CENTRAL BANK GOVERNORS REPORTED THAT THEY HAD AGREED ON) SOME IMPORTANT TECHNICAL IMPROVEMENTS IN THE OPERATION OF THE EXCHANGE RATE MECHANISM: EXTENSION OF RENEWAL ARRANGEMENTS FOR VERY SHORT-TERM FINANCING: AVAILBILITY OF SUCH FINANCING

11. A VERY POOR INITIAL SUMMARY BY SIMONSEN WAS CORRECTED AND BOTH IS AND DELORS' PRESS CONFERENCE STATEMENTS LATER IN THE DAY WERE A REASOANBLY FAIR REFLECTION OF THE DISCUSSION. TWO FEATURES OF THE POOR SUMMARY WERE EGREGIOUS REFERENCES TO REALIGNMENTS AND AN ENTHUSIASTIC DEMAND FOR FURTHER STUDY OF THE USE OF THE ECU. OVER LUNCH IT WAS AGREED TO DROP BOTH.

PREPARATION OF WASHINGTON MEETINGS

12. THE DRAFT PRESIDENCY STATEMENT WAS BROADLY AGREED, ALTHOUGH SOME FURTHER CHANGES MAY BE PROPOSED BY THE PRESIDENCY NEARER THE TIME. THE DISCUSISON FOCUSSED ON DEBT OF THE POOREST COUNTRIES. THE CHANCELLOR PLACED HIS OWN SUB-SAHARA PROPOSALS AND THE IMF PROPOSALS FOR ENLARGEMENT OF THE STRUCTURAL ADJUSTMENT FACILITY IN THE SAME STRAGTEGY AND SUGGEST BOTH BE PURSUED. HE WELCOMED THE SIMILAR VIEW EXPRESSED IN A COMMISSION PAPER. OTHERS WHO SPOKE FAVOURED THE IMF PROPOSALS, ALTHOUGH SEVERAL PROBLEMS WERE MENTIONED. ONLY AMATO (ITALY) GAVE FULL SUPPORT TO THE INTEREST RATE ABATEMENT PROPOSAL BY THE CHANCELLOR, BUT OTHERS AGREED THAT THERE SHOULD BE FURTHER DISCUSSION IN THE PARIS CLUB.

TAX APROXIMATION

13. OVER A SEPARATE LUNCH FOR MINISTERS ONLY THE CONCLUSIONS OF THE MORNING MEETING WERE SETTLED AND ALSO THE PROCEDURE FOR HANDLING TAX APPROXIMATION AS DESCRIBED IN THE SUMMARY.

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WAS A PRIOR NEED FOR FURTHER PROGRESS IN HARMONISATION OF STANDARDS AND SUPERVISION IN BANKING AND FINANCE, IN RIGHTS OF ESTABLISHMENT AND IN SOME AREAS OF TAX APPROXIMATION, THE CHANCELLOR AND OTHERS SPOKE STRONGLY AGAINST, WHILE FULLY ENDORSING THE DESIRABILITY OF ENCOURAGING PARALLEL ACTION TO REMOVE IMPEDIMENTS TO FREE CAPITAL FLOW APART FROM EXCHANGE CONTROLS. THE ONLY RESIDUAL WORRY WAS THAT OF DANISH MINISTERS, CONCERNING THE RISK OF LOSS OF DOMESTIC TAX REVENUES AS A RESULT OF EXPORT OF CAPITAL OUTSIDE THE DOMESTIC JURISDICTION AND SYSTEM OF REPORTING OF INCOME. FROM EXPERIENCE THE CHANCELLOR AND OTHERS ARGUED THAT LACK OF EXCHANGE CONTROL WAS NOT A DECISIVE FACTOR IN SUCH REVENUE LOSS, AND THAT COMPENSATING COMMUNITY-WIDE REPORTING SYSTEMS, ETC, WOULD NOT SOLVE THE PROBLEM OF TAX HAVENS OUTSIDE THE COMMUNITY. POOS (LUXEMBOURG) SPOKE VERY STRONGLY ON THE THEME THAT LIBERALISATION WAS THE KEY, THAT WE SHOULD AVOID COMPREHENSIVE HARMONISATION WHICH WAS A RECIPE FOR INTERMINABLE ARGUMENT, AND AVOID THE ASSOCIATED BUREAUCRACY.

8. THERE WERE WIDER DIFFERENCES OF REACTIONS TO THE CONCEPT OF SAFEGUARD CLAUSES, INCLUDING A COMMISSION PROPOSAL TO EXTEND WHAT THEY ARE ADVISED IS THE LEGAL COVERAGE OF PRESENT ARRANGEMENTS, BUT NO ATTEMPT WAS MADE TO PRESS THE DEBATE.

9. THERE WERE SOME IMPORTANT COMMENTS ON THE 1972 DIRECTIVE FROM STOLTENBERG (NO NEED TO RETAIN IT), RUDING (IT SHOULD BE ABOLISHED BECAUSE IT IS A WRONG TRACK FROM WHICH WE SHOULD NOW TURN BACK), AND THE CHANCELLOR (OUT OF DATE: WE COULD CHECK IF ANY OF IT WAS STILL RELEVANT AND INCORPORATE SUCH ELEMENTS ONLY IN THE PROPOSED NEW DIRECTIVE).

10. DELORS GAVE HIS OWN CONCLUSIONS: THAT LIBERALISATION SHOULD BE IMPLEMENTED AS SOON AS POSSIBLE AND NEED NOT AWAIT TAX AND OTHER HARMONISATION: THAT THE 1972 DIRECTIVE WAS OUT OF DATE, ALTHOUGH IT REMAINED IN HIS VIEW AN OPEN QUESTION WHETHER THE COMMUNITY NEEDED A CAPACITY FOR COLLECTIVE REACTION TO EXTERNAL PRESSURES EITHER WAY: THAT TAX QUESTIONS WOULD NEED TO BE PURSUED BECAUSE OF THE EXISTING WIDE DISCREPANCIES WHICH COULD BECOME MORE DAMAGING IN A CONTEXT OF NO EXCHANGE CONTROLS: AND THAT THE FINANCIAL SUPPORT MECHANISMS SHOULD BE REVAMPED, PERHAPS WITH SOME ARRANGEMENT TO USE THEM POSITIVELY TO FOSTER LIBERALISATION.