PREM 19/1419

PART 2.

A/21

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Retail and Wholesale Milk Prices.

AGRICULTURE

Part 1: May 79

Part 2: March 81

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
~~18.3.81~~		~~13.1.84~~					
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~~4.12.81~~		~~1.2.84~~					
~~7.12.81~~		~~7.2.84~~					
~~10.12.81~~		~~9.2.84~~					
~~14.12.81~~		~~22.2.84~~					
~~21.12.81~~		~~11.4.84~~					
~~26.3.82~~		~~13.4.84~~					
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PART 2 ends:-

Conservative Research Dept. brief 28.6.84

PART 3 begins:-

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TO BE RETAINED AS TOP ENCLOSURE

Cabinet / Cabinet Committee Documents

Reference	Date
CC(84) 20th Meeting, item 3	24/05/1984
CC(84) 4th Meeting, item 4	02/02/1984
OD(84) 6	21/02/1984
C(84) 2	26/01/1984
E(A)(84) 1st Meeting, item 2	19/01/1984
E(A)(84) 1st Meeting, item 2 Most Confidential record	19/01/1984
E(A)(84) 2	13/01/1984
EQS(84) 3	09/01/1984
E(81) 38th Meeting	10/12/1981
E(81) 31	13/03/1981
E(81) 32	17/03/1981
E(81) 11th Meeting	19/03/1981
E(81) 128	07/12/1981
E(81) 30	11/03/1981

The documents listed above, which were enclosed on this file, have been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate **CAB** (CABINET OFFICE) CLASSES

Signed J. Gray Date 18/11/2013

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DEBATE ON MILK QUOTAS AND THE AGRICULTURAL SETTLEMENT

It is hoped that this comprehensive brief will help Members during the above Debate as well as answering correspondence from constituents.

28th June 1984

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SETTLEMENT OF COMMON AGRICULTURAL POLICY PRICES FOR 1984/85 AND RELATED MEASURES

1. The Council of Ministers (Agriculture) agreed on CAP prices for 1984/85 and other related measures on 31 March. Most elements of the overall agreement are set out in the explanatory memorandum on draft instrument 6059/84 submitted by the Ministry of Agriculture, Fisheries and Food on 27 April. This note supplements this information in certain respects, notably on the budgetary implications and the agreement of principle on the conditions justifying the imposition of guarantee thresholds. Additionally, certain background information is included in the Annexes:-

(i) a note on "green" rate devaluations and revaluations is in Annex I;

(ii) a comprehensive list of the prices agreed for CAP commodities is in Annex II;

(iii) a list of the guarantee thresholds now fixed for certain agricultural commodities is in Annex III;

(iv) a table of the price effects of the package in individual member states is in Annex IV.

2. This year's price-fixing negotiation took place against the background of the decision by Heads of Government meeting in Stuttgart in July 1983 that the Common Agricultural Policy should be adapted to changing circumstances. The Commission's ideas for change were set out in document 8823/83 (explanatory memorandum submitted by the Ministry of Agriculture, Fisheries and Food on 14 September 1983), which were debated in the House of Commons on 1 December 1983. These formed the principal basis of the

Commission's price and other proposals for 1984/85 set out in draft instrument 4326/84 (several explanatory memoranda of 23 February 1984 refer).

Budgetary Implications

3. There will undoubtedly be substantial savings in the 1984 budget (that is calendar) year as a result of the introduction of a quota/supplementary levy scheme in the milk sector and the overall reduction in common prices of about 0.5 per cent, compared with the expenditure that would have been incurred if these measures had not been taken. The full savings will however only be realised in 1985 and subsequent years. However, the Commission estimate that some other parts of the package notably the agri-monetary arrangements will lead to additional expenditure. The carrying-over of some 675 million ecu of 1983 expenditure into 1984, and recent developments in agricultural markets will also affect the final position. The precise effects will also depend crucially on the stocks policy adopted by the Commission. If intervention stocks are allowed to increase Community expenditure will fall in the short-term but increase in the longer-term because intervention purchases are financed by member states in the first instance but the costs of their disposal falls on the Community. If intervention stocks are reduced the contrary applies.

4. Concern was expressed in the Council of Ministers about the difficulties the Community could face in keeping CAP expenditure within the 1984 budgetary provision of 16,500 million ecu. In particular the Commission stated that supplementary financing would have to be provided to cover EAGGF Guarantee expenditure in 1984 in excess of budget appropriations and that they expected the Council to take the necessary decisions to ensure the financing of the Community budget. The Commission said that would at a later stage come forward with detailed proposals in the Council for covering extra financial needs in 1984. (This they did on 18 April and the proposals are expected to be discussed in the Council of Ministers (Foreign Affairs) at its meeting on 14/15 May 1984).

5. In the Council of Ministers the Minister of Agriculture, Fisheries and Food made clear the Government's view that expenditure

on the Common Agricultural Policy in 1984 must be accommodated within the existing budgetary provisions. In the Government's view if budgetary problems arise later in the year (or in 1985) then the Commission and/or the Council (acting on a proposal from the Commission) should take the necessary steps to reduce expenditure to the permitted level.

Green Rates

6. The Council agreed a number of green rate changes set out in detail in Annex I. The background to the new agri-monetary arrangements agreed in the settlement is given in paragraphs 20 - 23 and 47 - 48 of the explanatory memorandum on document 6059/84.

Guarantee Thresholds and Similar Measures

7. In the settlement the Council agreed in principle to introduce Guarantee Thresholds as the Commission had suggested namely for products in or likely to be in surplus, and products on which expenditure is rising rapidly taking into account concessionary arrangements for imports from third countries.

8. Thresholds are short-term production targets for particular commodities set for the whole of the Community. They may operate in different ways but, broadly, if the target is exceeded action is triggered to discourage production, for example by abating support levels. The agreement reached on Guarantee Thresholds opens the way for the support for several CAP commodities to be curbed in the future which is potentially highly significant.

9. More specifically the Council agreed new guarantee thresholds for durum wheat, dried grapes, tomato products and sunflowerseeds. Cereals, oilseed rape, milk and cotton already come under varying systems of guarantee thresholds. It could be argued that similar measures already apply in the sugar sector where producers contribute to the costs of marketing production in excess of a certain level. Details of these thresholds and the way in which they are applied are given in Annex III below.

AGREED GREEN CURRENCY RATE CHANGES 1984/85

Member State	Old green rate, as at 31 March 1984 (1 ecu =	New green Rate (1 ecu =)	Percentage devaluation (-) revaluation (+)	Date at which new green rate takes effect
Belgium/Luxembourg	44.9008	46.4118 BF/LF	- 3.3	#
Denmark	8.23400	8.841499 DKR	- 2.2	#
Federal Republic of Germany				
Milk	2.54273	2.41047 DM	+ 5.5	1 January 1985
Cereals	2.52875	2.39792 DM	+ 5.5	1 January 1985
Other products	2.51457	2.38516 DM	+ 5.5	1 January 1985
France				
Milk	6.55400	6.93793 FF	- 5.5	2 April 1984
Wine/pigmeat	6.77297	7.10590 FF	- 4.7	pigmeat 1 November 1984 wine 1 September 1984
Other products	6.49211	6.86866 FF	- 5.5	#
Greece	77.2479	90.5281 DRA	- 14.7	#
Ireland	0.725690	0.750110 £IR	- 3.3	#
Italy	1341.00	1432.00 LIRE	- 6.4	#
Netherlands				
Milk	2.73327	2.71620 NFL	+ 0.6	1 January 1985
Cereals	2.72149	2.70178 NFL	+ 0.7	1 January 1985
Other products	2.70981	2.68749 NFL	+ 0.8	1 January 1985
United Kingdom	0.618655	0.618655 £UK	0	na

= beginning of marketing year for each commodity see Annex II

ANNEX I

COMMODITY	COMMON EC PRICE LEVEL: EUROPEAN CURRENCY UNITS (ECU)	COMMON EC PRICE LEVEL: £(1)	1984/85 MARKETING YEAR
MILK			
Target price for milk	274.30 ecu/tonne	17.47 p/litre	2 April 1984
Coresponsibility levy (3% of target price) (2)	8.229 ecu/tonne	0.524 p/litre	-
Intervention price for butter (82% fat)	3197.0 ecu/tonne	1977.84 /tonne	31 March 1985
Skimmed milk powder	1658.8 ecu/tonne	1026.22 /tonne	
BEEF AND VEAL			
Guide price	2050.2 ecu/tonne	1268.37 /tonne	2 April 1984 -
Intervention price	1845.2 ecu/tonne	1141.54 /tonne	31 March 1985
PIGMEAT			
Basic price	2033.30 ecu/tonne	1257.91 /tonne	1 November 1984 - 31 October 1985
SHEEPMEAT			
Basic price (3)	4280.4 ecu/tonne	2648.1 /tonne	2 April 1984 -
Intervention/guide price (3)	3638.3 ecu/tonne	2250.9 /tonne	31 March 1985
CEREALS (4)			
WHEAT			
Target price	259.08 ecu/tonne	160.28 /tonne	}
Reference price for breadmaking wheat (medium quality) (5)	213.14 ecu/tonne	131.86 /tonne	}
Common intervention price	182.73 ecu/tonne	113.05 /tonne	}
BARLEY, MAIZE AND SORGHUM			} 1 August 1984 -
Target price	236.30 ecu/tonne	146.19 /tonne	} 31 July 1985
Common intervention price	182.73 ecu/tonne	113.05 /tonne	}
RYE			}
Target price	238.37 ecu/tonne	147.47 /tonne	}
Intervention price	184.58 ecu/tonne	114.19 /tonne	}
DURUM WHEAT			
Target price	357.70 ecu/tonne	221.29 /tonne	1 July 1984 -
Intervention price	312.08 ecu/tonne	193.07 /tonne	30 June 1985
RICE (4)			1 September 1984
Target price for husked rice	539.49 ecu/tonne	333.76 /tonne	-
Intervention price for paddy rice	314.19 ecu/tonne	194.38 /tonne	31 August 1985
SUGAR (6)			1 July 1984
Basic price for sugarbeet	40.89 ecu/tonne	25.30 /tonne	-
Intervention price for white sugar	534.70 ecu/tonne	330.79 /tonne	30 June 1985
DRIED FODDER (7)			1 April 1984
- Guide price	177.15 ecu/tonne	(8)	-
- Flat rate of aid	8.41 ecu/tonne	5.20 /tonne	31 March 1985
FIELD BEANS AND DRIED PEAS (9)			1 July 1984
Minimum purchase price	289.0 ecu/tonne	178.79 /tonne	-
Activating price	512.4 ecu/tonne	(10)	30 June 1985
Guide price	331.1 ecu/tonne	(10)	
SWEET LUPINS (9)			1 July 1984
Minimum price	317.9 ecu/tonne	196.67 /tonne	-
Activating price	478.2 ecu/tonne	295.84 /tonne	30 June 1985
FRUIT AND VEGETABLES			
Withdrawal prices (seasonal scales) (11)			
Cauliflowers	5.88 - 17.35 ecu/100kg	3.64 - 10.73 /100kg	1 May 1984 - 30 April 1985
Tomatoes	8.02 - 14.61 ecu/100kg	4.96 - 9.04 /100kg	11 June 1984 - 30 November 1984
Apples	4.92 - 16.87 ecu/100kg	3.04 - 10.44 /100kg	1 August 1984 - 31 May 1985
Pears	5.26 - 19.39 ecu/100kg	3.25 - 12.00 /100kg	1 July 1984 - 30 April 1985
Peaches	10.02 - 39.68 ecu/100kg	6.20 - 24.55 /100kg	1 June 1984 - 30 September 1984
Sweet Oranges	9.97 - 26.96 ecu/100kg	6.17 - 16.68 /100kg	1 December 1984 - 31 May 1985
Mandarins	21.77 - 31.15 ecu/100kg	13.47 - 19.27 /100kg	16 November 1984 - 28 February 1985
Lemons	18.46 - 30.30 ecu/100kg	11.42 - 18.75 /100kg	1 June 1984 - 31 May 1985
Table grapes	9.23 - 17.17 ecu/100kg	5.71 - 10.62 /100kg	1 August 1984 - 31 October 1984
Apricots	21.86 ecu/100kg	13.52 /100kg	1 June 1984 - 31 July 1984
Aubergines	6.28 ecu/100kg	3.89 /100kg	1 July 1984 - 31 October 1984

COMMODITY	COMMON EC PRICE LEVEL		1984/85 MARKETING YEAR
	EUROPEAN CURRENCY UNITS (ECU)	£(1)	
OLIVE OIL			
Production target price	3162.3 ecu/tonne	1956.37 /tonne	1 November 1984 - 31 October 1985
Intervention price (4)	2276.2 ecu/tonne	1408.18 /tonne	
Production aid for 9 member states	695.6 ecu/tonne	430.34 /tonne	
OILSEEDS			
Colza and rape seeds (4)			
Target price	472.6 ecu/tonne	292.38 /tonne	1 July 1984 - 30 June 1985
Intervention price	429.2 ecu/tonne	265.53 /tonne	
Sunflower seed (4)			
Target price	582.2 ecu/tonne	360.18 /tonne	1 August 1984 - 31 July 1985
Intervention price	532.7 ecu/tonne	329.56 /tonne	
SOYA BEANS			
Guide price	570.1 ecu/tonne	352.69 /tonne	1 September 1984 - 31 August 1985
Minimum price	501.7 ecu/tonne	310.38 /tonne	
LINSEED			
Guide price	548.6 ecu/tonne	339.39 /tonne	1 August 1984 - 31 July 1985
TABLE WINE			
Guide price for type RI	3.42 ecu/degree hl	2.12 /degree hl	1 September 1984 - 31 August 1985
RII	3.42 ecu/degree hl	2.12 /degree hl	
RIII	53.30 ecu/hl	32.97 /hl	
AI	3.17 ecu/degree hl	1.96 /degree hl	
AII	71.02 ecu/hl	43.94 /hl	
AIII	81.11 ecu/hl	50.18 /hl	
TOBACCO (NORM PRICE)			
Badischer Geudertheimer	3.759 ecu/kg	2.326 /kg	1 January 1984 - 31 December 1984
Badischer Burley E	4.604 ecu/kg	2.848 /kg	
Virgin D	4.491 ecu/kg	2.778 /kg	
Paraguay and similar varieties	3.507 ecu/kg	2.170 /kg	
Nijkerk	3.463 ecu/kg	2.142 /kg	
Misionero/Rio Grande	3.227 ecu/kg	1.996 /kg	
Bright	3.951 ecu/kg	2.444 /kg	
Burley I	2.906 ecu/kg	1.798 /kg	
Maryland	3.313 ecu/kg	2.050 /kg	
Kentucky/Moro di Cori/Salento	2.741 ecu/kg	1.696 /kg	
Forchheimer Havanna/Nostrano del Brenta/Resistente/Gojano	3.415 ecu/kg	2.113 /kg	
Beneventano/Brasile Selvaggio	1.844 ecu/kg	1.141 /kg	
Xanti Yakà	3.645 ecu/kg	2.255 /kg	
Perustitza/Samsun	3.452 ecu/kg	2.136 /kg	
Erzegovina	3.101 ecu/kg	1.918 /kg	
Round Tip/Scafati/Sumatra I	16.410 ecu/kg	10.152 /kg	
Basmas	5.775 ecu/kg	3.573 /kg	
Katerini/Bashi Bagli	4.852 ecu/kg	3.002 /kg	
Kaba Koulak Classic/Elassona	4.302 ecu/kg	2.661 /kg	
Kaba Koulak Non Classic/ Myrodata Smyrnis/Phi I/Trapezous	3.321 ecu/kg	2.055 /kg	
Myrodata Agrinion	4.257 ecu/kg	2.634 /kg	
Zychnomyrodata	4.445 ecu/kg	2.750 /kg	
Tsebelia	4.032 ecu/kg	2.494 /kg	
Mavra	3.935 ecu/kg	2.434 /kg	
Burley GR	2.260 ecu/kg	1.398 /kg	
Virginia GR	3.387 ecu/kg	2.095 /kg	
FLAX AND HEMP			
Flax flat rate of aid	351.57 ecu/ha	217.50 /ha	1 August 1984 - 31 July 1985
Hemp flat rate of aid	319.29 ecu/ha	197.53 /ha	
SILKWORMS			
Subsidy per box	107.59 ecu/box	66.56 /box	1 April 1984 - 31 March 1985
COTTON			
Guide price	941.4 ecu/tonne	582.40 /tonne	1 August 1984 - 31 July 1985
Minimum price	894.4 ecu/tonne	553.33 /tonne	

COMMON EC PRICE LEVEL				
COMMODITY	1984/85		1985/86	
	EUROPEAN CURRENCY UNITS (ECU)	£ (1)	EUROPEAN CURRENCY UNITS (ECU)	MARKETING YEAR
SEEDS FOR SOWING				
Production Aid (12)				
Spelt Wheat	11.0 ecu/100kg	6.80 /100kg	11.0 ecu/100kg	
Rice (14)	14.6 ecu/100kg	9.03 /100kg	14.6 ecu/100kg	
Textile flax	21.6 ecu/100kg	13.36 /100kg	21.6 ecu/100kg	
Linseed	17.1 ecu/100kg	10.58 /100kg	17.1 ecu/100kg	
Hemp (14)	15.6 ecu/100kg	9.65 /100kg	15.6 ecu/100kg	
Grasses:				
Velvet Bent	60.8 ecu/100kg	37.61 /100kg	60.8 ecu/100kg	
Red Top	60.8 ecu/100kg	37.61 /100kg	60.8 ecu/100kg	
Creeping Bent	60.8 ecu/100kg	37.61 /100kg	60.8 ecu/100kg	
Brown Top	60.8 ecu/100kg	37.61 /100kg	60.8 ecu/100kg	
Tall Oatgrass	51.3 ecu/100kg	31.74 /100kg	51.3 ecu/100kg	
Cocksfoot	41.6 ecu/100kg	25.74 /100kg	41.6 ecu/100kg	
Tall Fescue	45.0 ecu/100kg	27.84 /100kg	45.0 ecu/100kg	
Sheeps Fescue	32.7 ecu/100kg	20.23 /100kg	32.7 ecu/100kg	
Meadow Fescue	32.7 ecu/100kg	20.23 /100kg	32.7 ecu/100kg	
Red Fescue	28.2 ecu/100kg	17.45 /100kg	28.2 ecu/100kg	1 July - 30 June
Italian Ryegrass	16.1 ecu/100kg	9.96 /100kg	16.1 ecu/100kg	
Perennial Ryegrass:				
High persistence	26.7 ecu/100kg	16.52 /100kg	26.7 ecu/100kg	
Low persistence	14.6 ecu/100kg	9.03 /100kg	14.6 ecu/100kg	
New varieties and others	20.8 ecu/100kg	12.87 /100kg	20.8 ecu/100kg	
Hybrid Ryegrass	16.1 ecu/100kg	9.96 /100kg	16.1 ecu/100kg	
Small Timothy	40.9 ecu/100kg	25.30 /100kg	40.9 ecu/100kg	
Timothy	66.9 ecu/100kg	41.39 /100kg	66.9 ecu/100kg	
Wood meadowgrass	29.7 ecu/100kg	}	}	
Smooth Stalked Meadowgrass	29.7 ecu/100kg	} 18.37 /100kg	} 29.7 ecu/100kg	
Rough Stalked Meadowgrass	29.7 ecu/100kg	}	}	
Leguminous plants:				
Field bean (13)	0 ecu/100kg	0 /100kg	0 ecu/100kg	
Field pea (13)	0 ecu/100kg	0 /100kg	0 ecu/100kg	
Trefoil	24.3 ecu/100kg	15.03 /100kg	24.3 ecu/100kg	
Lucerne (Ecotypes)	16.2 ecu/100kg	10.02 /100kg	16.2 ecu/100kg	
Lucerne (Varieties)	26.7 ecu/100kg	16.52 /100kg	26.7 ecu/100kg	
Egyptian Clover (14)	35.0 ecu/100kg	21.65 /100kg	35.0 ecu/100kg	
Alsike Clover	35.1 ecu/100kg	21.71 /100kg	35.1 ecu/100kg	
Crimson Clover (14)	35.0 ecu/100kg	21.65 /100kg	35.0 ecu/100kg	
Persian Clover (14)	35.0 ecu/100kg	21.65 /100kg	35.0 ecu/100kg	
Red Clover	38.6 ecu/100kg	23.88 /100kg	38.6 ecu/100kg	
White Clover	54.1 ecu/100kg	33.47 /100kg	54.1 ecu/100kg	
White Clover (Ladino)	54.1 ecu/100kg	33.47 /100kg	54.1 ecu/100kg	
Common vetch	23.8 ecu/100kg	14.72 /100kg	23.8 ecu/100kg	

NOTES

(1) Prices in sterling have been calculated at the representative rate of 1 ecu = £0.618655. The results have been rounded and sterling equivalents are approximate.

(2) Coresponsibility levy to be raised from 2% to 3% of target price for one year only, 1984/85.

(3) Prices vary according to a seasonal scale.

(4) Prices are for first month of marketing year. Prices are subject to monthly increments.

(5) The minimum quality reference price will be fixed at a level not exceeding 196.75 ecu/tonne.

(6) In the UK the A quota minimum beet price is £25.76/tonne and the intervention price for white sugar is £338.28 /tonne.

(7) Aid is paid at a flat rate of 8.41 ecu/tonne. Supplementary aid is paid when the world price of dehydrated fodder falls below a guide price (177.15 ecu/tonne). Supplementary aid will be paid on artificially-dried and eligible sun-dried products at 100% and 50% respectively of the difference between the world and guide prices.

(8) No sterling equivalent to guide price. Only the supplementary aid, when payable, is convertible into national currencies.

[illegible] For dried peas, field beans and sweet lupins (for which varieties are expected to be specified in the detailed regulations) used in the manufacture of animal feedingstuffs, aid is paid at rates equal to 45%, 45% and 60% respectively of the difference between the activating price and the world price of soya bean meal; for dried peas and field beans used for human consumption, aid is to be paid at a rate equal to the difference between the guide price and the average world market price for human consumption dried peas and field beans. In both cases, aid is only payable to operators who guarantee that the producer of dried peas, field beans and sweet lupins has received not less than the minimum purchase price.

(10) No sterling equivalent to activating price or guide price; only minimum price and rate of subsidy, when payable, are convertible into national currencies.

(11) Compensation determined for pilot varieties of specified size, grade and presentation: compensation for other varieties derived from this.

(12) The table shows rates of seed production aid for the 1984/85 and 1985/86 marketing years. These rates were fixed in 1983 under the 2-year price fixing arrangements. The conversion rate to be used to calculate the amount of aid in sterling is the representative rate applicable on 1 July of the marketing year concerned.

(13) Field beans and field peas remain in the list of aided species but at a zero rate.

(14) Since these species cannot be certified within the UK, production aid is not payable.

CAP PRICE CHANGES SINCE UK ACCESSION (MAIN COMMODITIES)

SETTLEMENT	AVERAGE ALL PRODUCTS (1)	MILK Target price	BEEF Guide price	PIGS Basic price	SHEEPMEAT Basic Price	WHEAT Milling/ bread (2) quality (3)	BARLEY Intervention price	RYE Intervention price	DURUM WHEAT Intervention price	RICE (paddy) Intervention price	SUGAR White Intervention price	OILSEED RAPE Intervention price	WINE (Type A.I White) Guide price	OLIVE OIL Intervention price
1 May 1973	+ 7.0%	+ 5.5%	+10.5%	+ 4.2%	-	+ 1.0%	+ 1.0%	+ 0.5%	+ 1.0%	+ 1.0%	+ 1.0%	+ 1.0%	+ 0.7%	+21.3%
[28 February 1974 = General Election]														
25 March 1974	+ 8.3%	+ 8.0%	+11.9%	+ 8.1%	-	+ 4.0%	- 0.1%	+ 4.0%	+41.3% (5)	+ 4.0%	+ 7.0%	+ 4.0%	+10.9%	+ 2.7%
19 September 1974	+ 5.0%	+ 5.0%	+ 5.0%	+ 5.0%	-	+ 5.0%	+ 5.0%	+ 5.0%	+ 5.0%	+ 5.0%	+ 5.0%	+ 5.0%	+ 5.3%	+ 5.0%
(Total 1974)	(+13.8%)	(+13.4%)	(+17.5%)	(+13.5%)	-	(+ 9.2%)	(+ 4.9%)	(+ 9.2%)	(+48.3%)	(+ 9.2%)	(+12.3%)	(+ 9.2%)	(+16.8%)	(+ 7.8%)
13 February 1975	+ 9.8%	+10.7% (4)	+ 8.5%	+ 8.6%	-	+ 9.0%	+ 9.4%	+12.0%	+ 8.8%	+ 8.0%	+15.0%	+11.0%	+ 8.1%	+50.8%
6 March 1976	+ 6.6%	+ 7.5% (4)	+ 8.0%	+ 8.0%	-	+ 4.0%	+ 4.5%	+ 3.5%	+ 6.0%	+ 6.0%	+ 8.8%	+ 8.0%	+ 6.4%	- 3.6%
26 April 1977	+ 3.6%	+ 3.5%	+ 3.5%	+ 5.0%	-	+ 3.5%	+ 3.5%	+ 4.0%	+ 0.5%	+ 4.5%	+ 4.4% (6)	+ 3.5%	+ 3.3%	- 2.2%
12 May 1978	+ 2.1%	+ 2.0%	+ 2.5%	+ 2.0%	-	+ 1.0%	+ 1.3%	+ 1.0%	NIL	+ 2.0%	+ 2.0%	+ 4.0%	+ 2.1%	+ 4.8%
[3 May 1979 = General Election]														
22 June 1979	+ 1.1%	NIL	+ 1.5%	+ 1.5%	-	+ 1.5%	+ 1.5%	+ 1.5%	+ 1.5%	+ 3.3%	+ 1.5%	+ 1.5%	+ 1.5%	+ 1.5%
2 June 1980	+ 4.6%	+ 4.0%	+ 4.0%	+ 5.5%	-	+ 4.25%	+ 4.5%	+ 2.5%	+ 4.5%	+ 6.9%	+ 5.3%	+ 4.0%	+ 5.5%	+ 4.0%
1 April 1981	+ 9.1%	+ 9.0%	+10.0% (9)	+11.0%	+7.5%	+ 5.5% (8)	+ 6.0%	+ 3.28%	+ 5.6%	+11.0%	+ 8.5%	+ 8.0%	+ 8.5% (7)	+ 9.0%
18 May 1982	+10.2%	+10.5%	+11.0% (10)	+10.5%	+10.5%	+ 7.5% (8)	+ 8.5%	+ 5.95%	+ 8.5%	+12.0%	+ 9.5%	+ 6.1% (11)	+11.0%	+11.0%
17 May 1983	+ 4.1%	+ 2.33%	+ 5.5%	+ 5.5%	+ 5.5%	+ 2.5% (8)	+ 2.96%	+ 2.96%	+ 4.6%	+ 5.5%	+ 4.0%	+ 4.0%	+ 6.0% (12)	+ 5.5%
31 March 1984	- 0.6%	NIL	- 1.0%	- 1.0%	- 1.0%	- 3.4% (8)	- 1.0%	NIL	NIL	+ 2.5%	NIL	- 2.0%	- 1.0%	- 1.0%

NOTES:
(1) Price changes relate to intervention (or equivalent) prices in ua or ECU weighted together by MAFF in proportion to the shares of each commodity in final agricultural production in the EC. The effects of transition are excluded.
(2) Up to 1975/76 = Intervention price, milling wheat; 1976/77 = Intervention price, breadmaking wheat; 1977/78 onward = reference price, breadmaking wheat.
(3) Since 1976/77, intervention available for feed quality wheat at barley price.
(4) In two stages, March and September.
(5) Effective increase + 26.7% allowing for reduction in production aid.
(6) Effective increase, allowing for change in basis of intervention price.
(7) + 10% for other types.
(8) Minimum quality breadmaking wheat. Figure not yet fixed for 1984/85; reduction will be at least 3.4%.
(9) 7.5% from start of marketing year, 2.5% from 7 December 1981.
(10) 8.5% from start of marketing year (20 May 1982), 2.5% from 6 December 1982.
(11) UK intervention price. A common intervention price is to be applied throughout the Community. In some areas the increases may be up to 8.5% because lower intervention prices have applied in previous years.
(12) +5-5% for other types.

GUARANTEE THRESHOLDS AND SIMILAR MEASURES AGREED IN SETTLEMENT OF 1984/85 CAP PRICES AND OTHER RELATED MEASURES

All Guarantee Thresholds Relate to 1984/85 Marketing Year

Product	Threshold Figure (million tonnes)	1983/84 Market Situation	Method of Application of Guarantee Threshold
All cereals except durum wheat	121.32	average production 1981-83 120.93 m tonnes	abatement of common prices if threshold exceeded.
Durum Wheat	4.60	average production 1979-82 4.39 m tonnes	1st year of operation action yet to be decided.
Oilseed Rape (colza)	2.41	average production 1981-83 2.41 m tonnes	abatement of common prices if threshold exceeded.
Sunflower Seeds	1.00	1983 production 1.0 m tonnes	1st year of operation action yet to be decided.
Milk	99.57	1983 deliveries 103.7 m tonnes	quota/supplementary levy scheme.
Currants	0.065	1983 harvest c 0.07 m tonnes	reduction of production aid payable if threshold exceeded.
Sultanas	0.093	1983 harvest c 0.1 m tonnes	" " "
Tomato Products	4.70	1982/83 production for processing 4.4 m tonnes	reduction of processing aid payable if threshold exceeded
Cotton	0.50	estimated 1983/84 production 0.43 m tonnes	reduction of production aid payable if threshold exceeded
		1983 production	
Sugar: White A	9.50	9.20	quota/producer coresponsibili
: White B	2.2	1.7	" " "
Isoglucose A	0.16	0.15	" " "
Isoglucose B	0.04	0.04	" " "

CAP SETTLEMENT: EFFECTS ON AVERAGE SUPPORT PRICES IN 1984/85 (1)

	Common price (ECU) change	Common price change plus effects of agreement on changes to MCA system		Common price change plus effects of all green rate devaluations since 1983/84 price-fixing		Forecast inflation 1984 (GDP deflator) (2)
		money terms	real terms (see col 6)	money terms	real terms (see col 6)	
	1	2	3	4	5	6
Germany	- 0.6	- 0.6	- 3.5	- 5.7	- 8.5	3.0
France	- 0.6	+ 2.7	- 4.3	+ 5.3	- 1.9	7.3
Italy	- 0.4	+ 3.0	- 6.7	+ 6.4	- 3.7	10.4
Netherlands	- 0.5	- 0.5	- 2.8	- 1.2	- 3.6	2.4
Belgium	- 0.6	+ 2.7	- 3.4	+ 3.9	- 2.2	6.3
Luxembourg	- 0.5	+ 2.8	- 4.3	+ 4.1	- 3.1	7.4
United Kingdom	- 0.6	- 0.6	- 5.2	- 0.6	- 5.2	4.8
Ireland	- 0.6	+ 2.7	- 5.1	+ 4.0	- 3.9	8.2
Denmark	- 0.7	+ 1.5	- 3.5	+ 1.5	- 3.5	5.2
Greece	- 0.5	+ 2.9	- 12.8	+ 16.7	- 1.1	17.9
EC average	- 0.6	+ 1.4	- 3.5	+ 2.2	- 2.7	5.1

(1) estimates prepared by Ministry of Agriculture, Fisheries and Food, based on intervention (or equivalent) prices. The price increases for each commodity for which prices are set under the CAP have been weighted together in proportion to the share of each commodity in final agricultural production in the European Community. The figures include the effects of transition.

(2) Source: EC Commission: European Economy November 1983

ANNEX IV

DAIRY PRODUCE QUOTAS REGULATIONS:

Section A: General points

A1	When will the regulations enter into force	As soon as they have been approved by both Houses of Parliament. Subject to Parliamentary timetable, expect this will be in mid-July.
A2	Haven't the regulations been put together with undue haste?	Many details have been subject to prolonged discussion in Brussels. Has been necessary to work quickly in order to make it possible for firm quota allocations to be given to all producers, including special cases, before first levy payments have to be made (in October-November) to comply with Community rules.
A3	What products will be covered?	The regulations will apply to all milk and milk products as defined in the Community legislation. At present this covers liquid milk, butter, cream and cheese, but if other products are added in the Community legislation they will be brought in here as well.
A4	How will theliquid milk equivalents of the various milk products be calculated?	The Commission regulation allows the quantities of milk actually used in producing products for direct sale to be stated for quota purposes where these

		are known. Where they are not, the Commission regulations provide automatic formulae for calculating the liquid milk equivalents of the products. For cheese, Member States may determine their own equivalence.
A5.	Will producers be allowed to exchange quota between direct sales and wholesale deliveries?	Not at this stage. We are considering what provision can be made, and will make separate provision for this in due course.
A6.	Can quota be sold or leased?	No. The Community legislation does not provide for this.
A7.	Would it not be better to allow quota to be freely sold or leased?	There would be certain advantages in this but at present it is not possible. At some time in the future it may be possible to seek agreement in Brussels to a more flexible system.
A8.	Can quota be transferred between producers by the MMB?	The Community legislation would enable us to give the MMB certain responsibilities for re-allocating quota which a producer has not used. But we do not believe it would be right to do this while the quota system is still settling in. This is one of the questions we shall be discussing with the industry in the next few months.

SEE ALSO SECTION D - LAND TRANSFERS

A9.	What is the difference between Formula A and Formula B?	Under Formula A (which will be operated in Northern Ireland) each producer is directly liable for supplementary levy, at 75% of the target price, on milk he delivers beyond his quota. Under Formula B (which will be operated in Great Britain) the first-hand purchasers of the milk - normally the MMBs - are liable for the supplementary levy, at 100% of the target price, on milk delivered to them beyond their quota: they have to pass the levy back to producers who exceed their quotas; but the rate of levy payable by these producers will be less than 100% because some producers will have delivered less than their quotas, thereby offsetting the excess produced by the others.
A10.	What will happen if the formula used in a region is changed?	Where formula A is implemented in place of formula B, individual producer quotas will not be changed, but producers will be required to pay levy to the Intervention Board instead of purchasers. In practice, MMBs are expected to act as agents for the Intervention Board so the only changes will be in the details of the calculation of levy payments.

Where formula B is implemented in place of formula A, producer quptas will again remain the same, and purchaser quotas will be calculated by aggregating the quotas of individual producers who deliver to each purchaser.

A11. How will quotas be altered if regional boundaries change?

If the whole of a holding in the old region is in the new region, its quota will be transferred entirely to the new regional wholesale quota. If changes in regional boundaries cut across holdings, the necessary proportionate changes will be made on a similar basis to the methods of quota calculation used for partial transfer of occupation of holdings.

A12. What will be the effect of quotas on farm rents?

Farm rents are in the first instance a matter for negotiation between landlord and tenant. In the absence of agreement there is provision for arbitration in accordance with a statutory rent formula in the Agricultural Holdings Act. Under both the existing Act and the Bill now before Parliament, the existence of quota arrangements will be a relevant factor which will be taken into account by arbitrator in determining the rent properly payable.

A13. Why is it that other Member States (particularly the Dutch and the Danes) have been able to implement the supplementary levy with much shorter regulations than our own?

Other Member States' constitutional and Parliamentary systems are different from ours. In particular, we are required to obtain Parliamentary approval for much more detail than elsewhere. In other countries the governments are generally given more freedom to prescribe detailed arrangements in administrative rules.

A14. What arrangements are being made for re-allocation of quota given up by outgoers?

The present Regulations do not cover this. The quota given up by outgoers will be kept in reserve while discussions continue as to how this quota should be re-allocated. Suitable provisions to cover the re-allocation will be introduced in due course.

A15. What do the Regulations mean by "primary quota"?

Primary quota is the basic allocation of quota calculated by reference to the producer's deliveries (or sales) of milk in the base year - i.e. normally 1983 for wholesale producers, and 1981 for direct sellers. It does not include any quota allocated under the special Case rules - SEE C6.

Section B: Allocation of Quota

B1.	Who will be eligible for a quota?	Quotas will be a located to holdings on which milk production was taking place on 2 April 1984.
B2.	What about somebody who stated after 2 April 1984?	If he took over the whole of a holding which was being used for milk production on 2 April 1984, the quota for that holding will pass to him (unless a different arrangements was agreed when he took over the holding). If he took over part of a holding he may be entitled to part of the quota - SEE SECTION D - LAND TRANSFERS If no milk production was taking place on the holding on 2 April 1984 there is no entitlement to quota. However, we shall consider any such cases on an individual basis if they produce documentary evidence to show that they were firmly committed to milk production prior to the adoption of the Community Regulations. The amount available for these cases will not be decided at this stage - there is no provision for them in the current Regulations.

B3.	How will quota be calculated?	For a <u>wholesale producer</u> (i.e. one who supplies the MMB) the normal basis will be his deliveries to the MMB during the 1983 calendar year, less 9%. For a <u>direct seller</u>, the normal base will be 1981 sales plus 1%.
B4.	What if a wholesale producer began milk production after 1 January 1983?	If he began before 1 April 1983, the basis will be his deliveries to the MMB during the 12 months 1 April 1983 - 31 March 1984, less 9%. If he has less than 12 months deliveries, i.e. he begun between 1 April 1983 and 31 March 1984, his actual deliveries during that period will be grossed up to give a 12 month figure (less 9%); in doing this grossing up calculation his deliveries in his first calender month of operation will be disregarded, and if he had only about 10 days' deliveries in that first month then the second month will be disregarded as well. If he began in late January, February or March, his April deliveries will also be taken into account.
B5.	What about a direct seller who started after 1 January 1981?	Similar arrzngements to those in B4 will apply, except that his sales in the base period will be reduced by 6% instead of 9%.

B6. What is the position of a direct seller whose business has altered since 1981?	If a producer's direct sales in 1983/84 were less than in 1981, his quota will be based on the actual level of 1983/84 sales. If his direct sales in 1983/84 were more than 6% above his sales in 1981, his quota will be based on his direct sales in 1983/84 less 6%, subject to a proviso that the result is not less than his direct sales in 1981 + 1%. SEE ALSO SECTION E.

Section C: Special cases

C1.	What are the Dairy Produce Quota Tribunals?	Three Dairy Produce Quota Tribunals (for England and Wales, Scotland, and Northern Ireland) are being set up to hear appeals on quota allocation and special case claims. Each tribunal (except the one for Scotland) will set up local panels to examine special case claims.
C2.	How will special case claims be processed?	Special case claims will be examined by the Ministry (in England) to see that prima facie they meet the conditions of eligibility. If the Ministery thinks they do not the producer can appeal to the local panel who will take the final decision. If the Ministry think the case is prima facie eligible for consideration, it will be passed to the local panel who will consider it. If the producer is unhappy about the panel's decision he can appeal to the Tribunal, who will take the final decision.
C3.	How will the Dairy Produce Quota Tribunals and local panels by constituted?	Except for Scotland, Dairy Produce Quota Tribunals and local panels will consist of up to seven members (including a Chairman) appointed bh Ministers. In practice, local panels will sit with a minimum of three members (in England). Rules of procedure will be determined by the Chairmen of the

Tribunal. For Scotland, the Tribunal will consist of twenty members appointed by the Minister, and will sit in panels of 3 members, each panel to choose its own Chairman.

C4.	How will consistency between decisions of local panels be ensured?	Dairy Produce Quota Tribunals will issue guidance to local panels on the criteria to be used in their decisions.
C5.	Will the Tribunals and local panels be able to consult outside experts?	Local panels will be able to consult anyone they consider able to help them, but (except in Scotland) the Dairy Produce Quota Tribunals will not, as they are bodies of appeal.
C6.	What do the Regulations mean by "secondary quota"?	Secondary quota is quota allocated under the special case provisions. Special case claims are of two sorts:

(i) "base year revision claims"

(ii) "development claims".

(i) relates to producers who have been affected by an "exceptional event (such as a natural disaster) in the normal base year, and are therefore entitled to have an alternative base year used to calculate their quotas;

(ii) relates to pr ducers who have carried out investments (whether under a Development Plan or not) to increase their milk output.

C7.	Will there be any minimum size below which special case claims will not be considered?	No minimum is prescribed for "exceptional event" applications. It will be for the Tribunal and local panels to decide how to deal with "exceptional event" claims, for example, what should count as a "natural disaster". In the case of development claims however, the first 7½% of expansion will be disregarded and only half the next 5% will be taken into account
C8.	Will all successful special case claimants be given all the quota they are asking for?	This depends on hpw many claims are successful. The first claims on the 2½% reserve for wholesale producers will be for base year revision claimants - i.e. those who have been affected by exceptional events. After they have been given the quota awarded to them, the rest of the 2½% reserve will be apportioned amont successful development claimants.

Section D: Land transfers

D1.	What happens to the quota when the occupier of a holding changes?	If the whole of the holding (ie all the land being used by the occupier, which may include both rented and owner-occupied land) passes to a new occupier, the whole quota goes with it unless the parties concerned agree otherwise. If a holding is divided, the general rule is that the quota will go to the part of the holding on which the dairy buildings are situated, unless all parties concerned agree otherwise. If they cannot agree, the interested parties will have the right to put a case to arbitration. The arbitrator may decide that the general rule (that the quota goes with the dairy buildings) should be varied so as to give a share of the quota to a part of the land which has no dairy buildings but has been used mainly for milk production in the last five years.
D2.	What records of quota will there be, and who will have access to them?	Registers of quota will be maintained by the MMBs giving details of holdings and their quotas. Individual entries will be open to inspection by any prlducer on that holding or any other person who can show he has an interest in that holding.

D3.	What will be the landlord's rights over quota relating to land which he owns?	Any problems are most likely to arise when there is a change of occupation of <u>part</u> of a holding.- particularly if the holding is partly owned by different landlords, or is partly owner-occupied and partly tenanted. In these circumstances the landlord's consent will be required for any apportionment of the qucta agreed between the old and new occupiers. The landlord will also have the right to see the entries relevant to his land in the quota register.

Section E: Direct Sales

1. Why is the base year for direct sales different from wholesale deliveries?	For wholesale deliveries, Community rules allow Member States to choose 1981, 1982 or 1983 as the base year, whereas for direct sales the legislation clearly specifies 1981 unless a producer has begun or greatly altered his production since 1981, when the base year us to be twelve months ending on 1st April 1984.
2. Why is the reduction only 6% for direct sellers who have a 1983/84 base year, compared with 9% for most wholesale producers.	Unlike wholesale deliveries, the Community rules do not allow Member States specifically to set aside a reserve from the national direct sales quota so specific account cannot be taken of this in the deduction.
3. Will there be any direct sales reserve?	Yes, but it will consist only of any unallocated quota and any quota surrendered by producers under the outgoers scheme.
4. Why do direct sellers have to apply for quota and also make a special case claim at the same time?	It has been possible to make initial quota allocations to wholesale producers because MMBs have records of individual deliveries, and then to determine any special case claims separately because there is a specific wholesale reserve. Direct sellers have to apply individually for quota because they will have to supply information on their individual sales

which can be used as a basis for calculating their quota. Because there will initially be no direct sales reserve, the procedure used for wholesale producers' special case claims cannot be used for direct sellers, but it has been possible to provide for handling the two applications in a single stage.

Section F: Wholesale deliveries: Miscellaneous

F1. Do individual wholesale producers have to apply for quota?	No - this is optional. The MMBs have already notified most producers of their provisional initial allocations; when the Regulations come into effect this will in most cases simply confirm the previous notification and the producer need do nothing. But if for example somebody has not already been given a provisional initial quota he will be able to make an application for quota. Also, the Regulations allow appeals to the Dairy Produce Quota Tribunal if a producer disagrees with his allocation.
F2. Do the Regulations lay down rules for the collection of the levy by MMBs?	No. This part of the Community legislation is directly applicable and therefore does not need to be covered in our Regulations. In practice, supplementary levy will be collected by the MMBs from wholesale producers by deduction from the monthly milk cheque.
F3. How will purchaser quotas be calculated (in regions to which formula B applies)?	Purchaser quotas will be calculated by aggregating the quotas of the individual producers who deliver to each purchaser.

F4.	How will producers be treated if they deliver to more than one purchaser?	Producer quotas will be calculated on the basis of their total deliveries to all purchasers. The corresponding purchaser quotas will be apportioned on the basis of the proportionate shares of deliveries to each purchaser; any supplementary levy will be calculated separately for the producer's deliveries to each purchaser.
F5.	Can refunds of over payments of levy be made?	The Regulations allow the Intervention Board to refund overpayments to MMBs and other purchasers, and for them to refund overpayments to individual producers.

MINISTRY OF AGRICULTURE FISHERIES AND FOOD

Jmb 19/6

PRESS NOTICE

WHITEHALL PLACE, LONDON SW1A 2HH.

Enquiries 01·233 8226
After hours 01·233 5550 Copies 01·233 5171
Switchboard 01·233 3000

[Joint Announcement by the Agriculture Departments in Great Britain]

June 19, 1984 MILK

DIRECT MILK SALES QUOTAS

A notice issued today by the Agriculture Departments in Great Britain, to milk producers who sell directly to the public says they will be asked to provide information on their direct sales of milk and cream, butter and cheese during 1981 and during the period April 1, 1983 to March 31, 1984.

The notice gives the following basis on which it is intended to calculate quotas though it says this may later need to be adjusted - up or down - when full information on the exact level of sales has been collected:

- the basic provision will be for a direct sellers quota to be set at the level of his direct sales in 1981 increased by 1 per cent.

However:

- if the producer's direct sales in 1983/84 were less than in 1981 the provisional quota would be set equal to the actual level of 1983/84 sales.

- if the producer's direct sales in 1983/84 were more than 6 per cent above sales in 1981 the provisional quota would be the quantity of direct sales in 1983/84 reduced by 6 per cent (except that no producer in this category would have a quantity lower than his direct sales in 1981 increased by 1 per cent).

There will also be provision for producers who have started making direct sales since 1981 and for special cases.

As soon as the United Kingdom regulations come into force producers who make direct sales will be required to register as direct sellers with the Milk Marketing Board (MMB), in whose area they are located, which will operate the administrative arrangements on behalf of the Intervent[illegible] Board for Agricultural Produce. Producers out with the board areas in Scotland will be required to register with the Department of Agriculture and Fisheries for Scotland.

Once all returns from producers have been received and the applications for special case treatment assessed, the total provisional requirements by producers for quota will be calculated so that the available national quota can be shared out. At this stage producers will be sent quota allocations.

At the end of the marketing year direct sellers will be asked to make returns in order to establish the level of their sales compared with their quotas. Levy will be payable at 75 per cent of the target price on sales in excess of quota. Payment will be required by July 31, 1985 for the whole of the 1984/85 marketing year in a single instalment.

These arrangements will apply on a United Kingdom basis. Producers who make both direct sales and wholesale sales will need both direct sales quota and wholesale quota.

NOTES FOR EDITORS

1. The introduction of a milk supplementary levy was agreed as part of the agriculture prices settlement at the EEC Council of Agriculture Ministers meeting on March 30/31, 1984. Mr Jopling's statement to Parliament on the meeting was given in Press Notice No 111 of April 2, 1984.

2. The supplementary levy is provided for in Council Regulations No (EEC) 856/84 and 857/84.

3. Mr Jopling announced to the House of Commons on May 25, 1984 arrangements which will enable the payment of compensation to farmers who wish to give up milk production. Details of his announcement were given in Press Notice No 184 of May 25, 1984.

4. Provisional details on wholesale quotas were issued on June 12 in Press Notice No 198.

Nicholas HORSLEY

(Dairy Trade Federation)

3/7

10 DOWNING STREET

From the Private Secretary

19 June 1984

I enclose a copy of a letter to the Prime Minister from Mr. Nicholas Horsley on behalf of the Dairy Trade Federation, in which he asks whether the Prime Minister would meet him, together with Sir Richard Butler and Sir Stephen Roberts to discuss the problems of the dairy industry. Mr. Horsley also enquires whether the Prime Minister might address the Federation's Annual Lunch on Tuesday 30 October this year.

I should be grateful for your Minister's advice on these two requests as soon as possible, and for a draft reply for the Prime Minister's signature. It is unlikely that the Prime Minister would wish to accept the speaking engagement at such short notice unless your Minister saw a very strong case indeed.

Could I please have your advice no later than 3 July.

(David Barclay)

Ivor Llewelyn, Esq.,
Ministry of Agriculture, Fisheries and Food

file

Soc

10 DOWNING STREET

From the Private Secretary

19 June 1984

I am writing on behalf of the Prime Minister to thank you for your letter of 15 June.

This is receiving attention and a reply will be sent to you as soon as possible.

(David Barclay)

Nicholas Horsley, Esq.

Northern Foods

15th June, 1984

Northern Foods plc, Beverley House, St. Stephen's Square, Hull, East Yorkshire HU1 3XG
Telephone: 0482-25432 Telex: 527149 NFOODS G Fax: Group 2 0482-226136

Mr. David Barclay
Prime Minister's office

As requested it would be helpful if any correspondence or telephone enquiries could be directed to the Northern Foods address.

Mr. Nicholas Horsley's private telephone number is Hull (0482) 224903

With Compliments

RPS R18

President
Nicholas Horsley
Director General
Michael Evans

Dairy trade federation

19 CORNWALL TERRACE LONDON NW1 4QP
TELEPHONE 01-486 7244 TELEX 262027

NH/KEV

15th June, 1984.

The Rt. Hon. Margaret H. Thatcher, M.P.,
Prime Minister,
10, Downing Street
LONDON SW1

Dear Prime Minister,

The Dairy Industry, from producer through to consumer, is going through a period of fundamental change.

Firstly, your Government has stated its intention to withdraw from control of the liquid milk market by the end of 1985 and we are all working on an alternative structure for the industry. Secondly, with the introduction of milk quotas, the availability of our raw material is being very substantially curtailed. For these two principle reasons I would make two requests.

Firstly, that you are kind enough to give Sir Richard Butler, President of the National Farmers' Union; Sir Stephen Roberts, Chairman of the Milk Marketing Board, and myself, half an hour of your time in the fairly near future. I am taking the initiative of fixing this meeting because it is well known of the hardship that milk producers are suffering, but very much less understood of the severe effect on employment and investment in the manufacturing sector of the dairy industry.

Secondly, I would like to ask whether or not you would be prepared to be the Guest Speaker at our Federation's Annual Luncheon, to be held on Tuesday, October 30th, at the Hotel Inter-Continental, London. This is normally a fairly short occasion, where the President of the Dairy Trade Federation and the principle guest each make about a ten minute speech. Traditionally, the Minister of Agriculture has attended, but in view of the serious changes facing our industry we felt we would at least be bold enough to approach you with this request.

Looking forward to hearing from your office,

Yours sincerely,

Nicholas Horsley

Nicholas Horsley
President

File - Mrs Vessey is writing

~~Andrew Turnbull~~ cc GA Ruth Rope

Pl. will you get M. Jopling's views.

FERB

14.6.

~~MR. BUTLER~~
MR. TURNBULL
~~MR. BARCLAY~~

I received a call from a Mrs. Catherine Vessey in Hull (0482 224903).

She is the Secretary to Mr. Nicholas Horsley, the President of the Dairy Trade Federation. Mr. Horsley, plus Mr. Stephen Roberts, President of the Milk Marketing Board and Sir Richard Butler, President of the NFU, wish to come and see the Prime Minister for half an hour to discuss the milk supply position as well as the position the Government is taking.

I explained to Mrs. Vessey that it might be a day or two until we can get back to her.

Advice please. David Barclay to deal in my absence.

CR.

14 June 1984

MR. BUTLER
MR. TURNBULL
MR. BARCLAY

cc Ruth ~~POPE~~ to keep an eye open pl.

1) Mrs Ryder 2) GR: to note

Mr Horsley will be writing.

Dms 14/6

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C

14 June 1984

File

AT

cc NO

CONFIDENTIAL

Ref. No: AG(84)10
Date: 29.5.84

Supplementary Brief

Outgoers Scheme

INDEX

Conservative Research Department,
32 Smith Square,
London SW1
Tel. 222 9000

Enquiries on this brief to:
Robbie Browne-Clayton

OUTGOERS SCHEME

MILK SUPPLEMENTARY LEVY/QUOTA ARRANGEMENTS

Reallocation Arrangements

1. Which type of small producer will benefit from the reallocation?

We are aiming specifically at producers with production below 200,000 litres - broadly those with less than 40 cows. In Northern Ireland the arrangement will be slightly different because of the very much higher proportion of small producers there. In England and Wales there are some 16,000 producers with less than 40 cows, and although they produce only 13 per cent of the milk they comprise 40 per cent of all producers.

2. How much quota is needed to restore them to 1983 levels?

About 160 million litres in England and Wales - 1¼ per cent of the total quota.

3. Why then are you trying to buy up 2¼ per cent?

Producers with less than 40 cows are first priority but there will be other categories of producer that we will wish to assist. We shall be giving further thought in the next few months to which categories should be helped next.

4. Is it not contrary to sound economics to give special help to small producers?

We are not seeking to interfere in any way with long term economic trends, which do not point to larger herds. All we are doing is removing the distortion of a 9 per cent cut in production for this category of producer.

OUTGOERS

5. What will be the conditions of the outgoers scheme?

Applicants will have to agree to surrender their quota in its entirety.

6. How will the 2¼ per cent ceiling be applied?

We shall be discussing with the interests concerned the best method of dealing with applications to ensure that the 2¼ per cent limit is not exceeded.

7. Will the scheme be open to very large producers? If so, does this not mean very large sums may be paid to some individuals?

Was this the flavour we wanted to give?

We have decided not to impose a top limit, because the urgent need is to get in enough quota to re-distribute to those we wish to help.

8. Will people who received payments under the old non-marketing scheme but later resumed milk production be eligible?

No. We shall not be accepting applications from people who benefitted from the old scheme.

9. How can you be sure successful applicants will not re-enter milk production?

Their quota will be cancelled, and it will not therefore be possible to sell milk from the holding concerned without incurring a liability for supplementary levy.

10. If somebody has just bought a dairy farm, will he be eligible for the outgoers grant?

We shall restrict eligiblity to people who have been in milk production continuously since 1 January 1983 - though not necessarily on the same holding for the whole time.

RATE OF GRANT

11. Why have you set the rate at £650 per cow?

The rate will actually be expressed as 13 pence per litre of quota surrendered - at a yield of 5,000 litres per cow this is equivalent to £650 per cow. We believe there will be many producers who very naturally feel uncertain about their future in milk production. We want to give them a reasonable incentive to take a decision now to leave dairying, thereby making more quota available for those who are determined to stay. We believe £650 is about right.

12. How will payments be phased?

In equal annual instalments over five years.

13. Will off-setting savings for the £50 million be found from agricultural expenditure?

The introduction of this scheme will have no consequences for ongoing policies this year. Future expenditure programmes are as usual a matter for consideration in the public expenditure survey.

EFFECT ON BEEF MARKET

14. Will not the extra cow culling have a depressing effect on the beef market?

We are of course aware that additional cow cullings are bound to have an impact on the beef market and we shall be keeping a very close eye on this sector. We shall also take careful account of this factor in framing the detailed arrangements for the outgoers scheme.

MECHANICS

15. What should producers do if they want to apply now?

Detailed arrangements for this will be announced shortly. Producers who wish to take advantage of the outgoers scheme will nedd to make applications to the Ministry. People who have gone out of milk production before their application is accepted by the Ministry will not be eligible.

16. If a tenant applies for the outgoers scheme, will his landlord have a veto?

Applicants will be required to declare either that they have the sole interest in the land or that they have obtained the consent of any person with any interest in the land.

CMO

File

Mr Turnbull
To see o/v.

CHIEF SECRETARY TO THE TREASURY

Treasury Chambers, Parliament Street, SW1P 3AG

Duty 29/5

Robert Lawson Esq
Private Secretary to the Minister for
Agriculture, Fisheries and Food
Whitehall Place
LONDON
SW1A 2HH

29 May 1984

Dear Private Secretary,

This is to confirm that after discussion on Wednesday and Thursday of last week it was agreed that there should be a milk outgoers scheme. It should be subject to a limit of £50m on overall cost. Grant per cow would be £650. Farmers should however only be eligible for the scheme if they go out of milk production altogether for 10 years.

With regard to the costs of the scheme, it was agreed that the Treasury would provide an additional £34m of which £10m would fall in the first year and £6m in each of the succeeding four years. The balance of the costs would be found by offsetting savings from agreed programmes. Finally, It was agreed that officials would pursue the question of propriety with regard to a call on the contingencies fund and the use of the Appropriation Act.

I am copying this letter to the Private Secretaries to the Secretaries of State for Scotland, Wales and Northern Ireland and to Andrew Turnbull at No 10.

Yours sincerely

Paul Pegler

P PEGLER
Assistant Private
Secretary

CONFIDENTIAL

File

da

bc NO

10 DOWNING STREET

From the Private Secretary

25 May 1984

Dear Ivan,

OUTGOERS SCHEME

At the House last night, the Prime Minister discussed the draft Answer on the outgoers scheme which was attached to your letter to me of 24 May. Also present were the Chief Whip and Mr. Alison.

The Prime Minister expressed a number of concerns on the draft. First, she felt that compensation for giving up milk production should be concentrated on smaller producers. The Government could be criticised if the scheme ended up making substantial payments to large producers with significant income from other sectors. There could be a repetition of the criticism of the payments made under the Wildlife and Countryside Act. Secondly, the undertaking to give up milk production and not return needed to be tightly drafted to prevent abuse. Thirdly, the time period during which outgoers were debarred from returning should be as long as possible, either twice the duration of the payments, or a minimum of ten years. The prohibition should continue under any successor to the present quota scheme. Fourthly, she was not convinced that for legal reasons it was impossible to impose a long period for staying out of milk production. The argument that this would be a restraint of trade seemed paradoxical when the proposals were in the context of a whole scheme which was a restraint of trade. Finally, she suggested that compensation payments should go only to those for whom milk was the sole or major activity.

The Minister of Agriculture said he accepted the validity of many of these points. In administering the scheme he too wished to give preference in granting applications for compensation to smaller farms and he wished to prevent outgoers from returning for as long as possible. As a matter of tactics, he wanted to avoid a statement in which all the details of the scheme appeared to be settled. The NFU had requested that detailed arrangements be left open for discussion. The reception the scheme received would be improved by leaving some matters open.

CONFIDENTIAL

/ A number of

da

A number of drafting changes were agreed - see attached sheet. The Prime Minister urged your Minister to ensure that the details of the scheme were tightly drafted to prevent abuse and that in practice preference would be given to small producers. On the period during which outgoers would be debarred from returning, your Minister agreed to look again at the legal advice, consulting the Attorney General as necessary.

I am copying this letter to John Gieve (HM Treasury), John Graham (Scottish Office), Colin Jones (Welsh Office), John Lyon (Northern Ireland Office), David Morris (Lord Privy Seal's Office), Janet Lewis-Jones (Lord President's Office), Murdo Maclean (Chief Whip's Office), Roger Bone (FCO), Alex Galloway (Chancellor of the Duchy of Lancaster's Office), Henry Steel (Law Officers' Department) and Richard Hatfield (Cabinet Office).

Yours sincerely
Andrew Turnbull

Andrew Turnbull

Ivor Llewelyn, Esq.,
Ministry of Agriculture, Fisheries and Food.

AMENDMENTS TO DRAFT ANSWER

Page 1: Para 3: Line 3

"... the payment of compensation particularly to those smaller enterprises seriously disadvantaged by the quota scheme who wish to give up milk production."

Page 1: Para 3: last sentence

"Those accepting compensation payments will be required to give an undertaking that they will give up milk production for at least as long as the quota scheme or any successor continues, and will not directly or indirectly return to milk production."

Page 2: Para 3: Line 5

Delete "requiring assistance".

SW

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's Private Office

Andrew Turnbull Esq
10 Downing Street
London
SW1

24 May 1984

Dear Andrew

... I enclose a copy of the Answer which my Minister intends to give announcing the introduction of an outgoers scheme for milk production. We now intend to put this down tomorrow morning.

Treasury officials would wish the last sentence of the third paragraph omitted. Their point is that the Chief Secretary's agreement to this scheme was on the understanding that producers receiving compensation payments would be required to stay out of milk production for at least 10 years. On the substance of this issue, my Minister is in full agreement with the Chief Secretary; it is his intention to ensure that anyone who benefits from this new scheme should be precluded from returning to milk production for as long as is legally and practically possible. For the moment, however, our legal advice is that it would not be safe under both Community and domestic law to go further than we do in this draft. It should be noted that the wording used in no way prevents us from requiring producers to stay out of milk production for a longer period, if a way of requiring this can be devised.

I am copying this letter to John Gieve (HM Treasury), John Graham (Scottish Office), Colin Jones (Welsh Office), John Lyon (Northern Ireland Office), David Morris (Lord Privy Seal's Office), Janet Lewis-Jones (Lord President's Office), Murdo MacLean (Chief Whip's Office), Roger Bone (FCO), Alex Galloway (Chancellor of the Duchy of Lancashire's Office) and Richard Hatfield (Cabinet Office).

Yours ever

Ivor

C I LLEWELYN
Private Secretary

/ Revised /

RESTRICTED

MILK SUPPLEMENTARY LEVY - OUTGOERS SCHEME

DRAFT ANSWER

I recognise that the introduction of the supplementary levy scheme presents special difficulties to small milk producers, particularly those who have no alternative to milk and who have little scope to adapt their dairy enterprises to a lower level of production under the quota scheme.

My aim is to make quota available as quickly as practicable to assist those small milk producers who wish to stay in milk. On the other hand, there are some milk producers who will wish in the new circumstances to give up milk production altogether.

In order to facilitate the release of quota the Government has decided to make funds available for the payment of compensation to those who wish to give up milk production. The compensation payments offered will be at the rate of £650 per 5000 litres of quota and this sum will be payable in equal instalments over 5 years. Those accepting compensation payments will be required to give an undertaking that they will ~~to~~ give up milk production for at least as long as the quota scheme or any successor continues, and will not directly or indirectly return to milk production. ~~In accepting applications preference will be given to smaller producers.~~

The quota released by the outgoers will be reallocated to those producers who wish to stay in milk. In England and Wales, my rt hon Friend and I intend to give priority to those who produced less than 200,000 litres in 1983 calendar year (about 40 cows) ~~and for whom milk production represented the sole or main activity~~. This group represents some 40 per cent of milk producers.

The aim will be to reallocate available quota so that producers in this category are able as soon as possible to return to their 1983 levels of sales without incurring supplementary levy. But the achievement of this objective will, of course, depend upon how much quota becomes available for reallocation from outgoers and how quickly it can be released.

Similar arrangements will operate in Scotland and Northern Ireland, though the details for reallocation of quota may differ.

There will be a limit of £50 million over five years on expenditure under this scheme in the UK which will enable up to 2¼ per cent of quota to be bought up in England and Wales, and Scotland; and up to 5 per cent in Northern Ireland where there is a greater concentration of small milk producers. ~~requiring assistance.~~ This expenditure will be contained within the planned totals of public expenditure. Community Regulations permit payments of compensation to milk producers who give up milk production. The necessary UK legislation will be sought as soon as possible.

We shall be consulting the interests concerned on the detailed arrangements for implementation.

010

cc PC

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

NO

From the Minister

The Rt Hon Peter Rees MP
Chief Secretary of the Treasury
HM Treasury
Parliament Street
London SW1P 3AG

23 May 1984

Dear Peter.

As you know from the discussions we have had in Cabinet and from your own contacts with the farming community, the milk quota arrangements agreed at this year's CAP price fixing are the subject of intense concern to all dairy farmers. This is by no means surprising, as the effect on the agricultural industry of CAP reform is inevitably very painful.

The introduction of the milk quota and super levy arrangements is expected to save the Community up to £1,000 million in 1984/85; the savings will be even greater in the next four years. Following the 1984 price fixing the Intervention Board now expects to spend some £300 million less on market support in the dairy sector in the UK in the 1984/85 financial year than it would otherwise have done. Moreover the impact of the price fixing on support for the UK dairy sector will carry through into succeeding years.

The impact of these measures on dairy farmers is naturally very sharp indeed. On average, wholesale producers in England and Wales will have to reduce their production by about 6½% compared with 1983, with a further 1% cut due next year. The effect is particularly severe on small producers who are mostly located in the South West, Wales and Northern Ireland where they have little or no alternative to dairy farming. These farmers' scope for reducing their overheads to maintain their profitability is negligible. Because of the relatively large number of small producers, their concentration in some areas and their importance to the rural economy their present difficulty is a particularly sensitive issue. The knock-on effect in the agricultural supply industry andin creameries in these areas of a significant collapse of dairy producers businesses would have serious implications for employment and the whole social fabric in these areas.

/ To alleviate the ...

To alleviate the worst effects for these producers, my agricultural colleagues and I believe we must take advantage of the restructuring provisions in Article 4(1)(a) of EEC Regulation 857/84 by providing assistance to those producers who wish to go out of milk production. We would propose to aim in effect to buy up to 2½% of the quota in England and Wales, and in Scotland; and up to 5% in Northern Ireland. This would represent some 423 million litres in total. The precise method of reallocating this would probably vary between England and Wales, Scotland and Northern Ireland to take account of the varying structure of dairying in these areas. In England and Wales it will be our intention to focus the aid on producers selling 200,000 litres of milk or less - equivalent to 40 cows - by restoring their production quotas towards 1983 production levels. Any surplus remaining would be used to top up the reserve quota established for special cases. Priorities for the use of this could vary in different areas of the UK.

If this scheme is to be effective a realistic purchase price for quota must be set. Our judgement is that a realistic price would be £750 per cow (equivalent to 5,000 litres) and on this basis the total cost of the scheme will be about £63 million. We have it in mind to pay the compensation over 5 years, though it may be desirable to load a rather larger proportion of the total onto the first year. Those producers who accept an outgoers payment will have to forego milk production for at least as long as the quota scheme continues.

As regards statutory cover for the scheme, it will not be possible to rely on the Communities Act and it will therefore be necessary to proceed under the Appropriation Act. Since it will be essential to implement this scheme immediately we shall also need Treasury agreement to recourse to the Contingencies Fund pending Parliamentary approval of the necessary Supplementary Estimate for the Agricultural Departments.

Other Member States are considering comparable action. West Germany has already announced a scheme under which they will be providing assistance to outgoers at an equivalent of £1,330 per cow(nearly double the rate we are proposing) and have set aside 1,000 million DM for this. The French are also known to be working on a package of measures providing assistance to producers. It has been reported that a package of measures costing some 3 billion FF will be provided.

The proposed assistance outlined above is modest in scale but and it would help defuse the growing political pressure we are all facing. This is something that we cannot properly ignore, particularly in relation to the European election campaign. The need for this measure arises, of course, directly from the milk quota and super levy arrangement agreed in the 1984 prices package and there is already in prospect the very large reduction in market support expenditure on the UK dairy sector to which I have referred above. My colleagues and I would ask you to accept that there should be no requirement to find further off-setting savings. This could only be achieved at the expense of support for other sectors already facing the consequences of the severe squeeze imposed by the last price fixing, including the cross effects on other sectors of the milk package.

I should be grateful for your agreement to proceed with this proposal as outlined above.

I am copying this letter to the Prime Minister, Jim Prior, George Younger, Nicholas Edwards and Sir Robert Armstrong.

James Prior

Michael

MICHAEL JOPLING

cc MASTER - change file title on master set

FILE

da

bc NO

10 DOWNING STREET

From the Private Secretary

18 May 1984

Dairy Industry

The Minister of Agriculture came to see the Prime Minister yesterday to discuss the problems of the dairy industry and to set out the case for an outgoers scheme. He said the long overdue adjustment in the dairy industry would have a serious impact on the small farmer in the West, particularly the tenant. Quotas had been cut by 9% from last year's level. He was looking for an arrangement which would ease pressure where it was strongest and he was considering proposals along the following lines.

Compensation would be paid at the rate of £150 per cow per year for five years to those who gave up dairying. There would be restrictions to prevent farmers who had left the scheme from re-entering. The aim would be to reduce production by two and a half per cent. The first one and a quarter per cent could be reallocated to small farmers to allow them to get back to 1983 levels of production. Herds of less than forty cows represented 37% of milk producers but only 13% of milk production. For a herd of this size the payments would provide income of £6,000 a year. Having dealt with small farmers any unallocated quotas could be used to help those who had not expanded between 1981 and 1983. The cost of such a scheme would be £12 million a year for five years. Your Minister hoped agreement could be reached on this scheme so that he could announce it next Friday.

The Prime Minister said she recognised the case for a scheme of this kind and she asked your Minister to discuss expenditure provision with the Chief Secretary. Given the pressures on public expenditure, she considered that part at least of the cost should be found from offsetting savings in the agriculture programme. Your Minister noted that the dairy agreement would save the Community £1 billion a year of which the UK's share would be over £200 million. What he was seeking was a small part of this saving.

/ I am

DCAABB

da

I am copying this letter to John Gieve (Chief Secretary's Office), John Graham (Scottish Office), Colin Jones (Welsh Office) and Derek Hill (Northern Ireland Office).

Andrew Turnbull

Ivor Llewelyn, Esq.,
Ministry of Agriculture, Fisheries and Food.

DCAABB

O10

CAP

SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

Prime Minister (2)
To note
AT 18/5

CONFIDENTIAL

A Turnbull Esq
Private Secretary
10 Downing Street
LONDON

18 May 1984

Dear Andrew,

MT

My Secretary of State understands that the Minister of Agriculture has spoken to the Prime Minister about the problems of allocation of milk quotas and the need for an outgoers scheme.

Mr Younger would like the Prime Minister to know that he shares Mr Jopling's concern over the intractable problems confronting milk producers and agrees that an outgoers scheme is unavoidable as a means of obtaining extra quota for redistribution among hardship cases. Such a scheme is provided for in the European Council regulations, and other Member States are implementing it. In Mr Younger's view no great expense should be involved, because the scheme should aim at being no more generous than is necessary to induce a relatively small number of the less committed producers to give up dairying. He considers that it would be wise to have separately administered schemes (although operating within a general similar framework) in Scotland and in Northern Ireland, because of the different structure of dairy farming there and also the different pattern of hardship cases.

I am copying this letter to the Private Secretaries to Secretaries of State for Northern Ireland and Wales and the Minister of Agriculture.

Yours sincerely

Eddie Gowans

EDDIE GOWANS
Private Secretary

Nick

CONFIDENTIAL

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's Private Office

NBPM
AT
13/4

MAFF Private Office confirm that the deal struck yesterday satisfied the condition at X
AT 13/4

Andrew Turnbull Esq
Private Secretary
10 Downing Street
London SW1

13 April 1984

Dear Andrew

MILK: QUOTA/SUPERLEVY SCHEME

David Williamson's minute to you of 12 April recorded that agreement was reached by Ministers - subject to legal advice - that the percentage reduction in quotas for England and Wales, Scotland and Northern Ireland should be the same. We have now consulted our legal adviser, and he is of the view that there is sufficient flexibility in the texts of the Community regulations to make it possible to construct a plausible case in favour of a solution on these lines, provided that, on the basis of the calculations worked out, Northern Ireland gets at least as much as it would have done if all the Regions had received 1981 plus 1% and Northern Ireland had, in addition, received 65,000 tonnes.

I am copying this letter to David Williamson and to the recipients of his minute.

Yours ever

Ivor

C I LLEWELYN
Private Secretary

AGRICULTURE: Milk Pt 2

CONFIDENTIAL

file. 54e

bc: W. Owen

10 DOWNING STREET

From the Private Secretary

MR. D. F. WILLIAMSON
Cabinet Office

Milk : Quota/Superlevy Scheme

The Prime Minister has seen and noted the agreement reached between the Agriculture Ministers after Cabinet on the allocation of quotas under the milk quota/superlevy scheme.

I am sending copies of this minute to Miss Lewis-Jones (Lord President's Office), Mr. Appleyard (Foreign and Commonwealth Office), Mr. Hill (Northern Ireland Office), Mr. Graham (Scottish Office), Mr. Jones (Welsh Office), Mr. Llewelyn (Ministry of Agriculture, Fisheries and Food), Mr. Maclean (Chief Whip's Office) and Mr. Hatfield (Cabinet Office).

AT

ANDREW TURNBULL

13 April, 1984

CONFIDENTIAL

ECL

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CC NO

CONFIDENTIAL

Qz.03675

Prime Minister

To note outcome of discussion of agriculture ministers - equality of misery but Northern Ireland is allowed to keep more of its recent increase.

AT 12/4

MR TURNBULL

MILK: QUOTA/SUPERLEVY SCHEME

Following the meeting of Cabinet this morning, there was a meeting attended by the Secretary of State for Scotland, the Secretary of State for Wales, the Minister of Agriculture, Fisheries and Food, the Minister of State, Northern Ireland Office and the Chief Whip in order to discuss the allocation of quotas under the milk quota/superlevy scheme to England and Wales, Scotland and Northern Ireland. Agreement has been reached - subject to legal confirmation that this result would be consistent with the Community regulations - that the percentage reduction in the quotas for England and Wales, Scotland and Northern Ireland should be the same. Northern Ireland would have an advantage from the special extra quota (65,000 tonnes of milk) because, despite the very considerable growth in milk production in Northern Ireland since 1981, it would only be cutting back by the same percentage as England, Wales and Scotland, which had increased much less.

2. The Secretary of State for Northern Ireland has confirmed that he can accept this agreement.

3. I am sending copies to the Private Secretaries to the Foreign and Commonwealth Secretary, the Secretary of State for Northern Ireland, the Secretary of State for Scotland, the Secretary of State for Wales, the Minister of Agriculture, Fisheries and Food, the Chief Whip and to Sir Robert Armstrong.

D F Williamson

D F WILLIAMSON

12 April 1984

CONFIDENTIAL

Confidential

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's Private Office

F E R Butler Esq
Principal Private Secretary
10 Downing Street
London SW1

11 April 1984

Dear Robin

My Minister met the Secretary of State for Scotland, the Secretary of State for Wales and the Minister of State in the Northern Ireland Office (Mr Butler) tonight to discuss the allocation of the United Kingdom milk quota to the various parts of the United Kingdom. The meeting was not able to reach any conclusions, and, in view of the urgent need to announce how the supplementary levy arrangements will be implemented in the United Kingdom, it was agreed that my Minister should raise this issue in Cabinet tomorrow.

My Minister said that the allocation of the Community quota to Member States had been based on 1981 production levels. This had penalised those countries, such as the United Kingdom, Germany and the Netherlands, which had expanded their production by more than the Community average since 1981, but it had been argued that the supplementary levy system was intended to bear with particular force on countries which had expanded production above the guarantee threshold set in 1981; despite our opposition this argument had prevailed. He would now be placed in a politically impossible position if he had to tell producers in England and Wales, who constituted 80% of the total number of the milk producers in the Unitred Kingdom, that different arguments were to apply where the division of the national quota within the United Kingdom was concerned, and that those who had expanded least, namely the producers in England and Wales, should have their production cut back by the same percentage as those that had expanded most. For these reasons, he believed that the Government had no option but to adopt 1981 as the base year for dividing the national quota within the UK.

Mr Butler could not accept an allocation based on 1981 for Northern Ireland. This would mean that Northern Irish milk producers would have to cut back their 1983 production level by some 10%, taking full account of the additional 65,000 tonnes obtained for Northern Ireland, whereas England and Wales would only have to reduce production by some 5.5%. This was clearly inequitable. It would also be politically impossible to impose on Northern Ireland the greatest reduction in the United Kingdom, given the strong arguments that the Minister himself had put forward for special treatment for Northern Ireland (at this stage, my Minister pointed out that Northern Ireland would obtain the full 4½% benefit of the additional 65,000 tonnes on their quota). Furthermore,

/ milk producers ...

milk producers in Northern Ireland were already at a disadvantage compared to their counterparts in Great Britain. 80% of their milk production went for manufacture, and they did not, therefore, benefit substantially from the higher returns from the liquid market. The only realistic alternative to milk production was beef, since 90% of Northern Irish milk producers were dependent on grass. However, beef producers in Northern Ireland had been particularly harshly hit by the new requirement to clawback beef variable premium paid on exports, since they exported a far greater proportion of their production than did those in other parts of the United Kingdom and producers would not benefit from the increases in the suckler cow premium announced for Great Britain, since this was already paid at the top rate.

The Secretary of State for Scotland was also opposed to the use of 1981. 1981 had been a particularly poor year in Scotland, and their share of total United Kingdom production in that year had been well below its normal level. In his view the only defensible course of action would be to use the latest production figures and spread the burden of the required reduction equally across the United Kingdom. This pointed to use of 1983 as the basis for allocation, as this achieved equal reductions for Scotland and England and Wales.

It was agreed that it was essential to inform producers of how the supplementary levy was to be implemented early next week at the latest. In view of this need for a rapid decision, the issue should be raised in Cabinet tomorrow.

You may find the attached table helpful; it shows the effects of using 1981 and 1983 as the basis of dividing the United Kingdom national quota, in terms of the cut backs from 1983 levels of production required.

I am copying this letter to Private Secretaries to Members of the Cabinet and to Sir Robert Armstrong.

Yours Sincerely
Ivor Llewelyn

C I LLEWELYN
Private Secretary

CONFIDENTIAL

Cutbacks required on 1983 deliveries of milk to dairies

	Base Year 1981	Base Year 1983
England and Wales	5.5%	6.6%
Scotland	8.4	6.6
Northern Ireland (without reserve)	14.8	6.6
(with reserve)	10.3	2.0
United Kingdom	6.6	6.6

CONFIDENTIAL

Prime Minister
It is clear from the letter below that this will be a contentious matter.
FERB 11.4

PRIME MINISTER

Cabinet: Community Affairs

Supplementary Brief

The Minister of Agriculture, Fisheries and Food may raise the question of the allocation of the milk quota to the different parts of the United Kingdom. This point is not agreed between the Minister and the Secretaries of State for Northern Ireland, Scotland and Wales. A minute from the Minister's Private Secretary to your Private Secretary is being circulated tonight but has not yet been received. We understand that the situation is as follows -

now attached

	If 1983 base were used	If 1981 base were used
England and Wales	-6.56%	-5.5%
Scotland	-6.56%	-8.4%
Northern Ireland	-2.07%	-10.3%

The special extra quota (65,000 tonnes) for Northern Ireland is included in these figures. The reserve for exceptional cases is not included because it would be constituted by the same percentage reduction from the quotas in England and Wales, Scotland and Northern Ireland: it does not therefore affect their relative positions.

D F Williamson

D F WILLIAMSON

11 April 1984

CONFIDENTIAL

E.R.

CUTBACK IN MILK DELIVERIES REQUIRED

Percentage reduction on 1983 deliveries.

	Using as Base		
	1981	1982	1983
England and Wales	-5.51	-6.01	-6.56
Scotland	-8.44	-7.07	-6.56
Northern Ireland *	-10.34	-7.06	-2.07
UK	-6.57	-6.57	-6.57

15½
5½
8½

* assuming 65,000 tons are allocated in full to Northern Ireland

E.R.

PRIME MINISTER

I understand that Mr. Jopling will be reporting to Cabinet tomorrow on the latest state of play on milk. Mr. Prior is away and the Northern Ireland Office have asked if Mr. Butler could attend for this item.

TIM FLESHER

11 April, 1984

& File

CDT

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's
Private Office

John Graham Esq
Scottish Office
Dover House
London SW1

11 April 1984

Dear John

As you know, a meeting has been arranged for 5.00pm this afternoon between my Minister, your Secretary of State, the Secretary of State for Wales and the Minister of State in the Northern Ireland Office, Mr Butler, to discuss milk quotas. My Minister believes that the United Kingdom's national reference quantity should be allocated to the various milk marketing boards on the basis of 1981 production levels.

... To help this discussion, I enclose tables which show the effects of basing the allocation on 1981, 1982 and 1983 production.

I am copying this letter and enclosures to Colin Jones (Welsh Office) and Will Haire (Northern Ireland Office).

Yours ever
Ivor

C I LLEWELYN
Private Secretary

SUPPLEMENTARY LEVY

1984/85 CUTBACK IN DELIVERIES REQUIRED USING 1981 AND 1983 BASES FOR QUOTA ALLOCATION

m.litres

		(i) 1983 deliveries	(ii) Quota allocation on 1981 base	using 1981 base (iii) Cutback required on 1983 deliveries (Col(i) - (ii)) m.litres	%	(iv) Quota allocation on 1983 base	(v) Cutback required on 1983 deliveries using 1983 base (Col (i) - (iv)) m.litres	%
England and Wales	1.	13,528	12,782	746	5.51	12,640	888	6.56
Northern Ireland	2.	1,402	1,194	208	14.84	1,310	92	6.56
	3.	1,402	1,257	145	10.34	1,373	29	2.07
AD MMB	4.	126	120	6	4.76	117	9	7.14
NS MMB	5.	68	58	10	14.71	63	5	7.35
S MMB	6.	1,193	1,091	102	8.55	1,115	78	6.54
Total Scotland	7.	1,387	1,270	117	8.44	1,296	91	6.56
UK	8.	16,317	15,245	1,072	6.57	15,245	1,072	6.57

NOTES : (i) Deliveries defined as in EC Questionnaire (ie includes wholesale sales to MMBs; Farmhouse cheesemakers' milk; and proportion of producer processor/ retailer milk)

(ii) 1983 deliveries figure provisional

(iii) Cols (iii) and (v) compare actual deliveries in 1983 calendar year with quota for 1984/85

(iv) NI figures in 3 above include reserve (about 63m litres)

ANNEX A.

SUPPLEMENTARY LEVY

ESTIMATE OF 1984/85 CUTBACK IN DELIVERIES REQUIRED USING 1982 BASE FOR QUOTA ALLOCATION

		m litres (i) 1982 Deliveries	(ii) % share of 1982 Deliveries	(iii) Quota Allocation on 1982 base	(iv) 1983 Deliveries	(v) Cutback Required on 1983 deliveries (col (iv) - Col (iii)) m litres	%
ENGLAND AND WALES	1.	13185	83.41	12,715	13,528	813	6.01
NORTHERN IRELAND	2.	1286	8.14	1,240	1,402	162	11.55
	3.	1286	8.14	1,303	1,402	99	7.06
AD MMB	4.	126	0.80	122	126	4	3.17
NS MMB	5.	66	0.42	64	68	4	5.88
S MMB	6.	1145	7.24	1,104	1,193	89	7.46
TOTAL SCOTLAND	7.	1337	8.46	1,289	1,387	98	7.07
UK	8.	15808		15,245	16,317	1072	6.57

NOTES: (i) Deliveries defined as in EC Questionnaire (ie includes wholesale sales to MMB); farmhouse cheesemakers' milk; and proportion of producer processor/retailer milk).

(ii) 1983 deliveries figure provisional.

(iii) NI figures in 3 above include reserve (about 63m litres).

MILK AND MILK PRODUCTS DIVISION I
9 April 1984

10 DOWNING STREET

THE PRIME MINISTER

9 April 1984

Dear Mr Hume

I fear that I may have misled you at Question Time on Tuesday by giving the impression that under the supplementary levy arrangements Northern Ireland would have scope to increase its milk production in the coming year above current levels. The additional 65,000 tonnes we obtained for Northern Ireland will reduce the impact of the supplementary levy there, but there will have to be some reduction in levels of production if the supplementary levy is to be avoided altogether.

Yours sincerely

Margaret Thatcher

John Hume, Esq., M.P.

10 DOWNING STREET

Prime Minister.

We have had to delay OD till 4.15 because the Foreign Secretary is making a statement on the EC Foreign Affairs Council.

You must end at 6.00 in order to change before Crown Prince Abdullah arrives at 6.30.

I fear it will be difficult to get through the OD agenda. Perhaps, therefore, if necessary the discussion of item 3 (milk super-levy) should be deferred.

A.J.C. 23/2.

E.R.

PRIME MINISTER

POLICY UNIT
22 February 1984

COMMON AGRICULTURAL POLICY: PROPOSED SUPPLEMENTARY LEVY ON MILK

Mr Jopling's efforts to negotiate a milk-tight super levy deserve support. On-farm milk quotas will be unpopular, and difficult to administer. They will force some dairy farmers to disband their herds and others to abandon their expansion plans. But both consequences have to be faced because the Community is 140% self-sufficient in milk.

The alternative is a substantial and sustained reduction in the price of milk. This was proposed by the UK; it would be a better solution in many ways, and should be kept on the table in Brussels, as a reserve in the event that a fair and effective super levy proves impossible to negotiate.

The worst feature of the quotas is that they will freeze the structure of the dairy industry. The partial remedy to this is a market in quotas: let those farmers who are tempted to go out of milk sell their quotas to those who wish to expand, or start herds. This will allow efficiency to increase without increasing milk production.

Nicholas Owen

NICHOLAS OWEN

Qz.03601

MR COLES

DEFENCE AND OVERSEA POLICY COMMITTEE, 22 FEBRUARY

--- I attach a brief for the Prime Minister on item 3: Common Agricultural Policy: Proposed Supplementary Levy on Milk (the "super levy").

2. The Secretaries of State for Northern Ireland, Scotland and Wales will be present for this item. The Minister of State (Mr MacGregor) will represent the Minister of Agriculture, Fisheries and Food and the Minister of State (Mr Lamont) will represent the Secretary of State for Trade and Industry.

3. I am sending a copy to Sir Robert Armstrong.

DF Williamson

D F WILLIAMSON

21 February 1984

Qz.03601

DEFENCE AND OVERSEA POLICY COMMITTEE, 22 FEBRUARY

BRIEF FOR THE CHAIRMAN

Item 3: Common Agricultural Policy: proposed supplementary levy on milk (the "super levy")

Background

1. This point has been added to the agenda at the request of the Lord President of the Council. In response to this a short paper (OD(84) 6) has been circulated by the Minister of State, Ministry of Agriculture, Fisheries and Food (Mr MacGregor) in the absence of the Minister of Agriculture, Fisheries and Food.

2. The milk surplus in the Community is very large. It is estimated that the level of Community self-sufficiency is about 127% and, if there were no subsidies on consumption, would be about 140%. More significantly, the rate of increase in milk production appears to have accelerated in 1983 and may well be substantial again in 1984. The milk surplus is the most important single cause of the budgetary problems of the Community; the 1984 budget provides for expenditure of 5006 million ecu (about £2900 million) on milk. The support for milk producers, by directing a very substantial part of the Community's budget to surplus disposal, is also a cause of the budget inequity from which the United Kingdom is the principal sufferer. A number of measures have been taken in recent years to reduce the cost to the Community of support for milk producers (in 1981 for example, Community expenditure on milk was reduced by over 1400 million ecu) and stocks were reduced to modest levels. In the last year the situation has deteriorated and some action is now imperative. The United Kingdom has argued for direct reductions in support prices but this has not proved to be negotiable in the Council of Ministers. A freeze on the target price for milk for 1984/85, however, has now been proposed by the Commission, this neutral effect being broadly achieved by a reduction of 11.4% in the intervention price for butter and an increase of 10.9% in the intervention price for skimmed milk powder.

/3.

3. In addition, the Commission had already proposed in its major package of common agricultural policy reforms (COM(83) 500 of 28 July 1983) that there should be a non-discriminatory super levy, payable by each dairy and passed back to each milk producer on any milk delivered in excess of his deliveries in a base year. The practical effect of the Commission's proposal is that each milk producer would have a quota which would be eligible for the full Community guarantee and above this quota the price received would be about 25% of the Community's target price for milk. This low price is the average commercial value of the Community's surplus milk (the Commission argue that the value of any further surplus milk is less than zero because it would cost the Community more to dispose of it than it would earn). There are considerable disagreements within the Community about the operation of the proposed quota/super levy scheme and, in particular, about the base reference figures. The Commission proposed, as the base figure, 1981 deliveries plus 1%, which would give a total of 97.2 million tonnes of milk in the Community.

4. The United Kingdom, recognising that the proposed milk quota/super levy is an essential element in the post-Stuttgart negotiations on the control of agricultural spending and hence of the budgetary negotiations, has said that we would be prepared to consider the super levy provided that it is legal, workable and non-discriminatory and that we are satisfied that it will be effective in obtaining the objective. Discussions are fully engaged in the High Level Group on Agriculture in Brussels on which Sir Michael Franklin represents the United Kingdom.

5. The United Kingdom's attitude to the package of CAP reforms was debated and approved in the House of Commons on 1 December. Following the latest price proposals the Minister of Agriculture, Fisheries and Food set out his position in paragraph 11 of his letter to the Prime Minister of 2 February (annexed). This letter was circulated to members of OD(E) and to the Secretaries of State for Northern Ireland, Scotland and Wales. The Cabinet Office requested that it should also go to the Lord President of the Council. This aspect of the proposals of the Minister of Agriculture, Fisheries and Food was accepted by his colleagues.

/He

He made it clear that the Government would need to consider its position if an acceptable supplementary levy (operating at the level of the farm and not of the dairy) was unattainable.

6. In the agricultural discussions now under way the United Kingdom's aims continue to be -

(i) to get agreement to the threshold level of 97.2 million tonnes as proposed by the Commission (although even this is well above consumption levels);

(ii) to set the base year against which quotas are judged by reference to 1983, not 1981 (this is almost certain to be attainable);

(iii) for the quota to operate at the level of the farm, not of the dairy, while leaving a limited amount of flexibility to deal with hardship cases;

(iv) to oppose any exemptions (Ireland is pressing for special treatment and Italy and Greece also did so in the European Council at Athens).

7. It is too soon to say whether we shall succeed in our aims and therefore whether a levy on terms acceptable to us can be negotiated. If changes of the sort described above can be achieved, then the damaging aspects of the levy referred to in paras 5 and 6 of OD(84) 6 would be greatly reduced. Any measures to reduce the milk surplus and its associated costs will inevitably cause hardship in particular cases. Much will depend on the nature and extent of the measures to deal with the hardship cases. It would be self-defeating if such measures were in a form which undermined the effectiveness of the super levy.

8. A meeting of the Sub-Committee on European Questions of the Defence and Oversea Policy Committee (OD(E)) has been arranged for 9.15 am on 8 March to consider outstanding issues on the 1984 CAP Price Fixing. It will have an opportunity to consider

/the

the latest position on the super levy proposal. A separate ad hoc meeting of the Ministers most closely involved in the post-Stuttgart negotiations has been arranged for 7 March to consider all the main aspects of the post-Stuttgart negotiations on 19-20 March. By then the likely form of a super levy, the place of the super levy proposal in the post-Stuttgart negotiations and the likelihood of a successful outcome on the various budgetary aspects will be clearer. It may then be easier to decide what final attitude the United Kingdom should take to the super levy proposal.

Handling

9. You may wish first to invite the Minister of State, Ministry of Agriculture, Fisheries and Food to introduce his paper, before inviting the Lord President of the Council to explain his concerns.

10. You may then wish to invite the Foreign and Commonwealth Secretary and the Chancellor of the Exchequer to explain how they see the super levy proposal in relation to the other aspects of the post-Stuttgart regulations. The Secretaries of State for Northern Ireland, Scotland and Wales may wish to comment.

Conclusions

11. You will wish the Committee to decide:-

(i) whether the United Kingdom should continue for the present to pursue its current line on the super levy proposals (para 11 of OD(84) 6);

(ii) whether the proposal should be reviewed further before the European Council on 19-20 March, and, in particular, whether it should be considered at the OD(E) meeting on 8 March which is to discuss the price fixing, when the results of the discussions in the High Level Group on Agriculture and in the Council of Ministers (Agriculture) will be clearer.

Cabinet Office

21 February 1984

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

CABINET OFFICE
A 801
2 FEB 1984
FILING INSTRUCTIONS
FILE No. 6/17/3.

The Rt Hon Sir Geoffrey Howe QC MP
Secretary of State for Foreign
and Commonwealth Affairs
Downing Street
London SW1A 2AL

2 February 1984

Dear Geoffrey

1984/85 AGRICULTURAL PRICES AND RELATED ISSUES

1. The Commission have recently produced their agricultural price proposals for 1984/85 and have confirmed the proposals for changes in the Common Agricultural Policy as set out in their post-Stuttgart document COM(83)500. The Agriculture Council will have its first discussion of this year's agriculture package on 6/7 February. I am writing to set out the line I propose to take on the major issues which I had the opportunity of outlining at Cabinet this morning.

2. My general approach will be to press for an early agreement in March. We shall need to feel our way on what agricultural issues should go to the European Council at its March Meeting. I shall make it clear that we see the financial guideline as an essential element in the budget settlement and, therefore, not for detailed negotiation in the Agriculture Council.

3. The financial background is that, following the increase of about 30% in expenditure in 1983, the FEOGA Guarantee Section budget has been set at some 16.5 billion ecu for 1984, (an increase of 4½% over 1983 provisional outturn). It is clear that it will be very difficult, if not impossible, for the Community to stay within this figure. This figure is based on the assumption that all the Commission's proposals are adopted within the envisaged timetable. This clearly is unlikely to happen. There are certain other assumptions underlying the Budget figures which now seem too optimistic.

/On the ...

4. On the financial guideline, the Commission acknowledge that "the intention" (ie their intention) of a growth rate of FEOGA Guarantee expenditure lower than the growth of own resources assessed using a three year moving average will not be met for 1983-85, since the predicted growth of expenditure is 11.1% against 6.8% for own resources. It would be virtually impossible to meet the Commission's objective given the growth in expenditure in 1983.

5. I shall argue strongly against increases in common prices and in the various premiums. Where market circumstances warrant it, we should argue for reductions in the common levels of prices and premiums. We shall need to take a clear position on this at next week's Council in order to counter the strong pressure which will undoubtedly come from some member states for larger increases than the Commission propose.

6. Another general point I shall emphasise is the need for decisions which are non-discriminatory between Member States. We must continue, for example, to resist any special concessions to the Irish, Italians and Greeks on milk. We shall also need to line up with the other Northern Member States in insisting that the negotiations should be concerned with Mediterranean products as well as milk and cereals. It will be politically essential that the final package is seen to be a fair and balanced one.

7. One of the main issues in this year's price fixing will be MCAs. Several member states want rules to be adopted for dismantling MCAs automatically. We should continue to argue against any approach which would base Community prices on the "strongest" currency, on the grounds that this would be inflationary and very costly in the medium term when the associated devaluations of the resulting extra negative MCAs work through the system. It seems likely, however, that the Germans and French will do some deal on this basis. If we have to give on this point later in the negotiations, we shall need to insist on the firmest rules we can get for regulating green rate devaluations.

8. On the related green rate proposals, the principal focus of negotiati will be the level of the "green" mark. The French and the Italians will strongly support the Commission's proposal that this should be substantially revalued, while the Germans have already indicated that they will vigorously oppose any revaluation. It is in our interests that the Germans should not be forced to revalue, since they would only do so if either or both of two conditions were met. The first would be that the change should be balanced by equivalent increases in common prices so as to avoid a decrease in farm prices in Germany in money terms; and the second that there should be provision for a system of offsetting national aids at least partly reimbursed by FEOGA. The Germans have successfully insisted on the first condition

/at recent ...

at recent price fixings. The possibility of the second was referred to in Commission's document COM(83)500, and we know the Germans have not wholly ruled this out. We must obviously avoid taking a line which would give the Germans an excuse for seeking increases in common prices; while the national aids approach would set an undesirable further precedent (there was a limited precedent in 1973/74), which could prove costly to FEOGA and would put pressure on us to provide similar aids when and if we decided to revalue. These disadvantages greatly outweigh the small savings to FEOGA from a German revaluation.

9. The rate for the "green" pound is of course important to us and especially to the farming industry. The 1984 White Paper on the outcome of the Annual Review of agriculture, which Ihave just circulated, shows a decline in farm income of 15% in money (19% in real) terms in 1983 to a level 10% (in real terms) below that obtaining when we came to office in 1979. Farmers face a further difficult year in 1984 given the need for painful adjustments to the CAP especially in the milk sector. A revaluation of the green pound by 4.2% as proposed by the Commission, would reduce producers' returns by £260m (in a full year) compared to total farm income of about £1540m in 1983. My department estimates that a revaluation by this amount would reduce farm income by about 10% from what it would otherwise have been. Taking account of the other economic decisions already taken* this year, it is clear that, with a revaluation of 4.2%, UK farmers would almost certainly face a further major decline in income in 1984. I believe that, both economically and politically, the problem with which this would present us would far outweigh any benefit that would be gained from the associated reduction in the retail price index of under 0.2% that would result from revaluation. Revaluation of the "green" pound is roughly neutral in terms of our contribution to the EC budget.

10. If we were to indicate a readiness to revalue, this would be bound to put extra pressure on the Germans to do so also, with the inevitable undesirable consequences I mention above. For all these reasons I am sure that our firm stance should be to oppose any revaluation of the green pound. This is essential domestically if I am to press for maximum restraint on common prices. I would use in the Council, if it seems helpful, the argument that it is wrong to treat floating currencies like sterling in the same way as those with fixed exchange rates. Only last year we had a negative MCA and could clearly do so again. Since it is essential that where "green" rates differ from market rates, MCAs should properly reflect different institutional price levels in the member states, we should continue to oppose the changes to the detailed rules put forward by the Commission post-Stuttgart which remain on the table.

11. On commodities we must ensure effective action to check the costs of the milk regime. We must continue to insist that any superlevy/quota scheme is fair, effective and non-discriminatory if it is to be acceptable to us; and that there should be no exemptions. In the context

/of a quota ...

of a quota scheme, we should continue to insist on a restrictive price policy. If, as I fear, price reductions are not negotiable, I should want to argue for a 3 year price freeze. This would depend on how effective any quota scheme was likely to prove to be. There is clearly a difficult negotiation ahead on this and we shall need to consider where we go if an acceptable on-farm supplementary levy is unattainable.

12. The other issue in the milk sector of political importance is the consumer subsidy for butter. Here the position is complicated by the Commission proposal to adjust the relationship between the support prices for the butter fat and skim components of the product. Although the Commission have proposed the abolition of the subsidy currently worth 14p/lb in the UK, the net effect on the consumer price of butter in the UK would (without revaluation) be an increase of about 3½p/lb. However, the subsidy is widely regarded as one of the few benefits the UK gains from the CAP and we cannot lightly give it up. Nor can we be certain that the shift in the butter/skim ratio will be agreed; there are substantial objections from the viewpoint of the increased costs of skim. I propose to take the line that any reduction in the butter subsidy would be an inappropriate response to the current market situation for butter. At a later stage, we may need to reconsider our line on this.

13. On cereals, we must press for the firmest possible commitment by the Council to a progressive narrowing of the gap between Community prices and prices in the main producer countries, together with at most a price freeze for 1984/85. We shall need to make it very clear that we see agreement on this (and on milk) as linked to any mandate for further discussions with the US on cereal substitutes. This will clearly be another difficult area of negotiation where the French will be pressing for early decisions. On the oils and fats tax, we must continue to take a very firm line (particularly as some of our Northern allies may be none too sound when we reach the later stages in the negotiations).

14. On beef, the Commission has proposed the abolition of the variable premium scheme (BVPS). This is preferred by producers to intervention as a means of support, and also provides considerable benefit to consumers. Although somewhat more expensive to the Exchequer than intervention, the benefit to consumers is much greater than the Exchequer costs. Moreover it has helped to keep beef out of the political arena. Our purchases into intervention in 1983 were under 20,000 tonnes; without BVPS, we estimate purchases would have amounted to nearly 100,000 tonnes. The substantial stocks implied by purchases of this order could only be disposed of to eastern Europe with the inevitable furore that such sales would cause. At the meeting on 6/7 February I shall, therefore, argue for the continuation of BVPS without changes such as clawback, drawing heavily on the argument that switching from BVPS to intervention would substantially increase the cost to FEOGA and therefore run counter to what we and the Commission are seeking to achieve.

/On sheepmeat, the ...

CONFIDENTIAL

15. On sheepmeat, the Commission have put forward some changes to the market regime. Our line must be to insist that producers in the UK should be supported to the same extent as producers elsewhere in the Community. This does not mean that we need resist changes in the regime. Indeed, we would like to secure some modification which would help our exports to other member states. I shall need to investigate what changes may be possible; but the French will be very difficult. At the same time, we should ensure that any changes to the Community's trading arrangements with New Zealand and other third countries are fully negotiated with the suppliers concerned.

16. On more general issues, I shall be guided by the agreed line taken before and at the Athens Summit. There are many other technical proposals which I suggest officials should look at.

17. I am copying this letter to the other members of OD(E), the Secretaries of State for Northern Ireland, Scotland and Wales, and to Sir Robert Armstrong.

Yours Ever

Michael.

MICHAEL JOPLING

CONFIDENTIAL

~~CE~~ N.O.

Treasury Chambers, Parliament Street, SWIP 3AG
01-233 3000

9 February 1984

The Rt Hon Michael Jopling MP
Minister of Agriculture, Fisheries and Food
Whitehall Place
LONDON SW1A 2HH

N.B.P.R.

A.J.C. 10/2.

Dear Michael

Many thanks for sending me a copy of your minute of ~~1~~ February to the Prime Minister on the Commission's threat to disallow certain FEOGA guarantee payments on milk.

I agree with your assessment of the situation, and with the action you are taking. The threat in respect of 1978 and 1979 expenditure seems to have disappeared, but for 1980 and subsequent years it remains very real, and time is short, for we shall presumably have to resolve matters - which may well entail legislation - well before the Commission close the 1980 and 1981 FEOGA accounts which they aim to do before the end of 1984. Like Geoffrey Howe - minute of 8 February - I should like to be kept in close touch with the negotiations in London and Brussels, and I suggest that officials from our three Departments should compare notes quickly on the timetable for decisions, and let us have an agreed "critical path".

Copies of this letter go to the Prime Minister, Geoffrey Howe, Michael Havers, Sir Robert Armstrong, and the other recipients of your minute.

Yours ever

Nigel

NIGEL LAWSON

CONFIDENTIAL

Agriculture : Milk
Pt 2

CC NO

N. B. P.R.

FCS/84/43

A.S.C. 8/2

MINISTER OF AGRICULTURE, FISHERIES AND FOOD

Milk Marketing Arrangements and FEOGA Disallowance

1. Thank you for copying to me your minute of 1 February to the Prime Minister.

2. I am sure you are right to set up talks with Dalsager, Tugendhat and Commission officials now that the 1978/79 accounts have been cleared. It would be helpful if you could keep me closely informed as the negotiations - at home and in Brussels - develop.

3. I have now also seen a copy of your letter of 2 February to Sir Stephen Roberts requiring the Milk Marketing Boards to discontinue, by the end of February, the practices which have led to the disallowance case. I look forward to knowing his reaction. I agree with you that it will be necessary to legislate if we cannot secure the voluntary cooperation of the industry.

4. I am copying this minute to the recipients of yours.

(GEOFFREY HOWE)

Foreign and Commonwealth Office
8 February 1984

cc NO

2

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's Private Office

Andrew Turnbull Esq
Private Secretary
10 Downing Street
London SW1

2 February 1984

Prime Minister
To note
AT
3/2

Dear Andrew

MILK MARKETING ARRANGEMENTS AND THREATENED FEOGA DISALLOWANCE

In his minute of 1 February to the Prime Minister, my Minister said that he would be seeing the milk industry leaders again to tell them formally that the pricing practices that have been challenged by the Commission must be brought to an end. I am now writing to inform you that my Minister saw Sir Stephen Roberts of the Milk Marketing Board and Mr Nicholas Horsley of the Dairy Trade Federation separately today and formally asked them to discontinue these pricing practices by the end of February. I enclose a copy of the letter my Minister handed to Sir Stephen Roberts; a similar letter was given to Mr Horsley.

I am copying this letter to Roger Bone (Foreign and Commonwealth Office), to John Grewe (H M Treasury), and to David Williamson (Cabinet Office).

Yours ever

Ivor

C I LLEWELYN
Private Secretary

Agriculture : Milk Prices Pt 2

-3 FEB 1984

-3 FEB 1984

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

2 February 1984

Sir Stephen Roberts
Milk Marketing Board

DR 3/2

Dear Steve

MULTIPLE PRICING OF MILK

The Commission have initiated action under Article 169 against some of the UK milk industry's pricing practices which they regard as being contrary to Community law, and in particular to the Regulations governing the Milk Marketing Boards.

The Commission have three main complaints:

(i) the setting of two prices for milk for manufacture into butter depending on whether the butter is to be sold in packets on the open market or manufactured in bulk, mainly for intervention. The Commission considers that there should be one price for milk for butter for all uses;

(ii) the setting of multiple prices for skimmed milk depending on whether the skim is to be manufactured into skimmed milk powder; sold in liquid form for stock feed with the aid of a Community subsidy; or used in high value products. The Commission consider that there should be one price for skim for all uses;

(iii) the setting of lower prices for milk to be manufactured into certain non-intervention products for export to third countries. The Commission believe that there should be one price for milk for each use and that additional differentation of this kind on the basis of destination is not permissible.

The first two complaints are now the subject of proceedings in the European Court of Justice (Case No. 23/84) and the Commission's reasoning is set out in detail in their application to the European Court. Their objections to export pricing were set out in a letter

before action under ...

before action under Article 169 dated 27 May 1983. These are not published documents, but have been made available to your organisation on a confidential basis. We would have no objection to the circulation of relevant extracts within your organisation provided their confidentiality is respected.

The Commission have now made a clear link between these pricing practices and FEOGA disallowance in the milk sector. Although the Commission have now decided against disallowance in respect of the 1978 and 1979 accounts, they have made it clear that this is without prejudice to their position in subsequent years. In view of the large sums of public money that are at risk if the Commission ~~were to~~ press the disallowance for subsequent years, I have to ask the dairy industry to make arrangements to discontinue indefinitely the practices complained of without delay. The industry has agreed to remove the dual pricing of butter. But this has taken an unacceptably long time through the arbitration procedure. I must ask you to remove the dual pricing of butter without further delay and to make arrangements to discontinue the remaining multiple pricing practices by the end of February.

This letter is without prejudice to our position in any existing or future legal cases.

I am writing in similar terms to Mr Horsley and copying my letters to Sir Richard Butler.

MICHAEL JOPLING

ccNO

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

Prime Minister (2)

Relevant to the Cabinet discussion.

AT 1/2

From the Minister

CONFIDENTIAL

PRIME MINISTER

1 February 1984

MILK MARKETING ARRANGEMENTS AND THREATENED FEOGA DISALLOWANCE

1. I sent you a minute on 13 January describing the threat of disallowance arising as a result of the Milk Marketing Boards' pricing practices. Nigel Lawson and Geoffrey Howe have also commented. In view of the gravity of the matter I thought it would be right to bring you up to date with developments.

2. The first point is that, as you know, the Commission machine has taken longer than anticipated to clear the 1978 and 1979 account and as a result the story has leaked. The Commission Legal Services have however produced a helpful opinion arguing that it would be wrong for the Commission to disallow expenditure in the milk sector, at least in 1978 and 1979, since the Commission led the United Kingdom to believe that the MMBs' practices were acceptable by recognising the MMBs under the terms of the Community regulation and not subsequently withdrawing recognition. I hope that the 1978 and 1979 accounts will be cleared in our favour when the Commission meet to-day although I understand they may not complete discussion until next Wednesday, 8 February.

3. Secondly, the Commission have now opened European Court proceedings against the United Kingdom in the butter and skim case.

4. Thirdly, I saw the industry leaders on 17 January and told them in complete confidence about recent developments. I said that the disputed pricing practices would now have to be brought to an end as quickly as possible. However, in view of the risk of a leak I asked them to regard what I had said as strictly confidential and told them not to consult their members until I had had an opportunity to speak to them again. I shall be seeing them separately over the next two days and telling them formally that the disputed practices must be brought to an immediate end despite the commercial cost to them. I shall indicate that we are prepared to legislate if necessary.

/5. Fourthly, our .....

5. Fourthly, our lawyers have further considered the possibility of bringing the disputed practices to an end by legislative means They have concluded that there is doubt as to whether we have powers to do this by domestic legislation. We are therefore in the process of seeking the Law Officers' views on whether Community law leaves the Government any scope for forcing an end to the practices in advance of a Court judgement; whether it would be safer to make primary legislation rather than an Order under the European Communities Act; and to what extent either would prejudice our case before the Court. However, my feeling is that we may have to take some risks on the legislative side if we are to bring to an end practices which are putting milk sector expenditure of £1 million a day in jeopardy. Nevertheless if we do this there will be a risk of challenge by our industry which could no doubt lead to a reference to the European Court.

6. Geoffrey Howe has suggested that we should open discussions with the Commission without delay with a view to exploring the possibility of a deal on the lines mooted in my minute of 13 January. I do not think it would be wise to embark on these delicate negotiations in advance of the clearance of the 1978 and 1979 accounts. Moreover given the legal uncertainties I would prefer to try and establish first whether the industry are willing to end the practices voluntarily - since this would be less prejudicial if a Court case has to be fought. However, as soon as the 1978 and 1979 accounts are cleared I shall arrange a without prejudice discussion with Mr Dalsager, Mr Tugendhat and appropriate Commission officials and explore the possibilities.

7. Nigel Lawson has emphasised that we should take a fundamental look at the present organisation of the Milk Marketing Boards and the powers they exercise. In my recent paper to Cabinet I have undertaken to conduct such an examination, but this will take time and I think it would be wrong to underestimate the risks and political difficulties of fundamental changes. This does not however rule out early changes to the Board's pricing practices.

8. I am copying this minute to members of E(A), the Foreign and Commonwealth Secretary, the Attorney General and the Secretary of the Cabinet.

MICHAEL JOPLING

Agric Milk Pt 2

E1 FEB 1984

PRIME MINISTER

POLICY UNIT
1 February 1984

LIQUID MILK PRICES AND THE FUTURE OF MILK MARKETING

I suggest two additional arguments against raising maximum milk prices at this time.

The dairy industry has behaved in an anti-competitive fashion, and risks court action as a result. An Office of Fair Trading investigation has unearthed 54 restrictive agreements, involving 56 dairies (including most of the major ones). The agreements involve prices, discounts, restrictions on supply and the allocation of milk rounds. These have not been registered with the Registrar of Restrictive Practices and are now void. It would be odd to grant a price increase to an industry while proceedings are being considered against a number of members of it.

The dairy farmers are not, contrary to the impression given by farming Ministers, expecting an increase. In the Autumn of last year they were expecting a substantial decrease. News of a standstill would be a relief for many of them.

The decontrol of milk prices raises a tactical consideration. Controls protect the consumer from the monopoly power of the marketing boards. Just to illustrate what this power means, a farmer wishing to supply milk directly to a dairy has to pay a levy to the MMB of 1½-4p per litre. This largely removes the incentive to offer cheaper milk, from locations close to centres of milk consumption. If decontrol precedes the dismantling of the marketing monopolies, consumers may be exploited. We can therefore expect (and welcome) increased pressure from consumers organisations for fundamental changes in the milk marketing arrangements. For this reason, it is important that Michael Jopling's examination of these arrangements must be a fundamental one with full involvement of interested departments.

NICHOLAS OWEN

Ref.A084/358

PRIME MINISTER

Liquid Milk Prices and the Future of Milk Marketing

Flag A C(84) 2

BACKGROUND

On 19 January the Minister of Agriculture, Fisheries and Food put proposals to the Ministerial Sub-Committee on Economic Affairs (E(A)) for increases in the maximum wholesale and retail prices of liquid milk in England, Wales and Northern Ireland (there is no control of milk prices in Scotland). Most members of E(A) took the view that a decision should be delayed until the likely outcome of discussions of milk prices and production within the European Community was clearer, and preferably when the results of a review of milk price control, which the Minister had already set in hand, were available. Since, however, the Minister had indicated that he might wish to refer the matter to the Cabinet, final decisions were not taken (E(A)(84) 1st Meeting, Item 2).

Flag B

Flag C

2. In C(84) 2, the Minister of Agriculture, Fisheries and Food puts forward his latest proposals. They have the following main features:

(i) As previously proposed, the maximum retail price of milk would be increased by 1p a pint. But the operative date would be 3 June 1984, not 4 March 1984.

(ii) The maximum wholesale price of milk would be increased by 0.58p per litre (0.33p per pint) from 1 March 1984, compared with the previous proposal of 0.91p per litre (0.52p per pint) from 1 February 1984.

(iii) These decisions would be announced immediately. The announcement would indicate that the Government intended to consult interested parties with a view to ending the control of milk prices by the end of 1985 at latest.

(iv) In accordance with the conclusions of E(A)(84) 1st Meeting, the Minister proposes to undertake an examination of the future marketing arrangements for milk and to bring forward recommendations for discussion by the summer.

3. These proposals compare as follows with those put to E(A):

(i) The 1p increase in the maximum retail price is deferred for three months. The increase in the maximum wholesale price is deferred for one month and is somewhat smaller.

(ii) So far as the distributors are concerned the combined effect by the end of March 1985 is the same as that under the Minister of Agriculture's earlier proposals, ie, they will be neither overpaid nor underpaid by that date. The fact that the increase in the wholesale price will now come three months earlier than the increase in the retail price means that their margin will actually fall during the period March to June, but they will still be in a position of overpayment during that period. And the smaller increase in the wholesale price means that they will do rather better than under the earlier proposals from early June onwards, so that the cumulative position is much the same by end March 1985.

(iii) The milk producers are somewhat worse off than under the earlier proposals because of the one month deferment of the wholesale price increase and the fact that it will be smaller (0.33p rather than 0.52p per pint).

(iv) The consumer benefits from the three month deferment in the retail price increase. On an annual basis the increase is 3.1 per cent rather than 3.7 per cent.

(v) Announcements would still be made forthwith, ie, before the likely result of negotiations within the Community was known.

(vi) The announcement would however now include an indication that the Government intended, after consultation, to abolish control of milk prices by the end of 1985 at the latest.

(vii) The need to review the existing arrangements, including the role of the Milk Marketing Boards (MMBs), and to involve other Departments in the review, is now accepted, but would not be referred to in the announcement.

Flag D

4. The factual background was set out in the brief submitted by Mr Gregson for the discussion in E(A): for convenience, I attach a copy. The basic information in that brief remains accurate, except that the later operative date of the retail price increase which is now proposed reduces the cost to public funds in 1984-85 (ie, the additional cost of intervention) from £20 million to £13 million.

MAIN ISSUES

5. The main issues are:

(i) The future of price control.

(ii) The size and timing of any price increases during 1984.

Price Control

6. It is probably common ground now that there is little justification for continued price control of milk. It is clearly out of line with the Government's general philosophy and, with the admission of milk imports and increased sales of milk in supermarkets, is no longer necessary to protect the consumer.

7. The remaining question is whether price control should be abandoned forthwith or whether, as the Minister of Agriculture now proposes, he should announce consultations with a view to abolition by the end of 1985. Most Ministers will probably take the view that it would be undesirable to abandon the system without preparation. The Minister of Agriculture presumably now feels less concern than he expressed earlier about the effect on

the future of doorstep deliveries. It may be that an early announcement, followed by a period of consultation, will meet his objective of gradual rather than drastic change.

Issues Relating to the Milk Marketing Boards

8. As you know, the Commission is pressing for changes in the pricing arrangements of MMBs; and it has been suggested that agricultural expenditure in 1978 and 1979 should be disallowed. The question of disallowance is entirely unrelated to the issues discussed in C(84) 2; and the Commission's objections to the pricing policies of the MMBs are directed at products other than milk for consumption in liquid form. However, the dispute is likely to arouse concern in the industry about the future of the MMBs, and generate public interest in their operation. The relationship between any announcement on the future of price control of liquid milk and the dispute with the Commission will need to be handled carefully.

9. In view of the discussion in E(A) it is unlikely that any member of the Cabinet will dissent from the proposed review of milk marketing arrangements. But some Ministers may wish to stake a claim to be consulted, or to register particular points that the review should take into account.

Size and Timing of Increases in 1984

10. If it is agreed that price control of liquid milk is to continue, albeit only until the end of 1985 at the latest, there is then the question of the size and timing of any increases in 1984. Most members of E(A) favoured delay in announcing any price increase for two main reasons. It seemed wrong to give further encouragement to the over-production of liquid milk; and for the United Kingdom to be seen to do so would weaken our position in the negotiations on the Common Agricultural Policy.

11. The Minister of Agriculture's revised proposals are still open to these objections. There are two main difficulties:

(a) The announcement of the Government's decisions would still be made at once.

(b) The price increase to producers, though smaller than proposed in E(A)(84) 2, would still be effective from an early date; it is, of course, the price paid to producers which is most relevant to discussions in the Community.

12. Against that, the Minister of Agriculture can be expected to argue that returns to milk producers have fallen sharply; that the Government should not use its exceptional powers to control milk prices in order to discriminate against milk producers; that under his proposals, liquid milk prices will still go up by less than in virtually any other Community country; and that the consequences of delay on morale in the industry, already apprehensive about the effect of imports and proposals, such as the "super levy", within the Community, would be serious.

Announcement

13. The content and timing of any announcement will depend on the decisions reached on the issues of substance. If it is decided to delay any announcement of price increases, the Cabinet will wish to consider whether the announcement of consultations about ending price control should also be delayed. You will no doubt wish the Minister of Agriculture to circulate the text of any public announcement to the Cabinet for clearance in correspondence.

HANDLING

14. You will wish to invite the Minister of Agriculture, Fisheries and Food to introduce his memorandum. The Secretaries of State for Northern Ireland and Wales could add any points affecting their countries. The Chancellor of the Exchequer could then be invited to reply. The Foreign and Commonwealth Secretary will have comments from the standpoint of negotiations in the Community.

CONCLUSIONS

15. You will wish the Cabinet to reach conclusions on the following:

(i) Should the maximum retail and wholesale prices of milk in England, Wales and Northern Ireland be increased as proposed in C(84) 2; or should decisions be delayed?

(ii) If prices are to be increased, should the announcement of that decision include an indication that the Government intends to consult interested parties with a view to removing the control of milk prices in England, Wales and Northern Ireland by the end of 1985 at latest?

(iii) Any points relevant to the proposed review of marketing arrangements for milk.

RTA

ROBERT ARMSTRONG

1 February 1984

10 DOWNING STREET

Prime Minister

Mr. Jopling is staying behind after the Rome briefing meeting. He would like an indication of whether a paper along the lines of the attached would be likely to command agreement in Cabinet.

It differs from the earlier paper

(i) The 1p increase is from June not March (giving more to distributors, less to producers)

(ii) There is now a firm intention to decontrol milk prices by 1985

(iii) He agrees to examine the marketing arrangements.

You may want to consider overnight, and avoid being manoeuvred into promising support.

AT 25/1

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's
Private Office

Andrew Turnbull Esq
Private Secretary
10 Downing Street
London SW1

25 January 1984

Dear Andrew

MILK PRICES

As you know, my Minister is hoping to have a word with the Prime Minister this evening about milk prices. Before this meeting, it would be most
... helpful if the Prime Minister could see the enclosed draft of the paper he is considering putting to Cabinet on this subject, as he intends to seek the Prime Minister's advice on whether a paper in this form would be likely to lead to agreement there.

Note
Told MAFF that
Prime Minister:
(i) recognised that these proposals were significant move
(ii) agreed paper should be circulated
(iii) would allow Mr Jopling to develop his case (but would not commit herself in advance to support).

Yours ever
Ivor

C I LLEWELYN
Private Secretary

CONFIDENTIAL

LIQUID MILK PRICES AND THE FUTURE OF MILK MARKETING MEMORANDUM BY THE MINISTER OF AGRICULTURE, FISHERIES AND FOOD

1. I am in disagreement with some of my colleagues over the handling of milk prices.

2. For a long time, Governments have controlled the price of milk to protect consumers, to stabilize prices so as to encourage consumption of liquid milk, protect the doorstep delivery system and reduce the amount of butter and skim milk powder going into intervention. Now that we are admitting imports of UHT milk, the need for price control to protect consumers will become less. I would like to get away from this piece of Government intervention, as has already happened in Scotland. But such a decision needs careful preparation and staging if we are not to destabilize the whole market. Nevertheless, I am prepared to enter now into consultation with the interests concerned with a view to bringing milk price control to an end within a reasonable period of time.

3. However, such a move is bound to raise wider questions about our milk marketing arrangements. In spite of derogations negotiated some years ago, the Milk Marketing Board (MMB) has never fitted easily into the Community milk regime. Its activities are now coming under intense legal and other pressure from the Commission, egged on by other member states who are greedy for a larger share of the historically open UK market. Changes in the Board's pricing arrangements will have to be made. This is in hand. These will be controversial enough but anything which appears to undermine the existence of the Board is bound to arouse immense opposition in the agricultural industry and Parliament. The

MMB's have long been regarded as the jewel in the crown of agricultural marketing. At risk is milk production in remote and hill areas; the availability of cheap fresh milk in the inner cities; and the whole regional balance of agriculture. I am willing to look at the issues involved but I am sure that we must proceed with the utmost circumspection if we are to avoid a major political row.

4. In the meantime, we must be ready to operate the present system. The retail price of milk last went up in November 1982. We avoided any increase last autumn. The latest review of the situation shows a sharp fall in producers' net margins to about half the level in the last 2 years of the Labour Government and an even more gloomy outlook for 1984/85. My proposal is to raise the retail price by a further 1p and then to hold it at that level until at least March 1985. My detailed proposals are at Annex A.

5. Against this proposal, colleagues have argued that:-

(a) a retail price increase is not yet justified, particularly as the distributors have been overpaid to date and will only move into deficit in the summer. But the figures of incomes and the results of the costings exercise fully justify what I have proposed. Indeed it is relatively modest given the fall in incomes this year. If the retail price increase is effective from 4 March I can distribute the effect roughly half to the producers and half to the distributors. If I delay the increase until the beginning of June the benefit to the producers will be correspondingly less.

(b) the proposed milk price increases would weaken our CAP negotiating position. I do not accept this. Liquid milk prices have been going up faster in most other Member States than in the UK and the average returns to our producers from milk sales are already lower than in most other Member States, reflecting our low butter and cheese prices. Although we must continue to fight hard in Brussels to get the CAP milk surplus down, I see no justification for unilateral action against our producers.

6. Our agriculture industry faces some tough prospects, especially on milk with the likelihood of a super levy, as we wrestle with the problems of the CAP. They are sufficiently realistic to accept this. But there is no point in alienating them unnecessarily. Not do we want to bring the whole pack of cards down on our heads. I therefore invite colleagues to agree:

(a) with my proposals for adjusting prices as set out in Annex A, but with the retail price increase effective from 3 June;

(b) that I should indicate, in announcing the changes, that the Government now intends to consult interested paties with a view to decontrol of milk prices by the end of 1985 at the latest;

(c) that I should examine the future marketing arrangements for milk in consultation with other Departments and bring forward my recommendations for discussion with colleagues by the summer.

ANNEX A

Detailed proposals

(i) a liquid milk retail price increase of 1p per pint from 4 March 1984. This would represent an annualised increase of only 3.7% compared with the Treasury estimate of a year-on-year inflation rate of around 5.5% in the first half of 1984: and I would not plan any further increase for the coming year;

(ii) a maximum wholesale price increase of 0.98p per litre (0.56p per pint) from 1 March - this would give producers a little over half of the proceeds of the retail price increase and should leave the distributors neither overpaid nor underpaid at the end of March 1985 (but with an agreement that if there is then an amount owing to or owed by the distributors it should be written off);

(iii) an increase in the dairy trade's target rate of profit, as established under the arrangements agreed with the Treasury in 1982, from 0.9048 ppl;

(iv) the issue of the Parliamentary announcement attached at Annex C.

Financial Implications

The effects on production and consumption will be very small. I expect them to add about £20m to the estimated cost of intervention in 1984/85 of £479m. This cost will of course be recouped when the produce is eventually sold.

CC NO

2

Prime Minister.

A.J.C. 23/1

FCS/84/18

MINISTER FOR AGRICULTURE, FISHERIES AND FOOD

Milk Marketing Arrangements and the Threatened Feoga Disallowance

1. Thank you for sending me a copy of your minute of 13 January to the Prime Minister. I have now also seen Nigel Lawson's minute of 17 January.

2. I entirely agree with the line you propose, and with all Nigel Lawson's points, including his last on the need for a fundamental look at the present organisation of the Milk Marketing Boards (MMB). I gather that E(A) has now decided on this.

3. I particularly welcome your suggestion that you have urgent discussions with the milk industry to persuade them to discontinue the pricing arrangements complained of, indicating if necessary that the Government would be prepared to legislate urgently if the industry are unwilling to make the changes voluntarily. As Ray Whitney said in his letter of 11 July last year to John MacGregor, while we cannot (short of legislation) require the Marketing Boards to show greater flexibility over pricing we can press them very hard on the consequences for British policy of rigidity (which could be grave indeed). I am pleased you now propose to do that. I understand that you met representatives of the MMB on 17 January, and look forward to hearing how your discussions went.

4. You note that we are facing very substantial financial risks 'that could not previously have been foreseen'. I feel bound to observe that when EQO discussed all this in June last year FEOGA disallowance was discussed as a real possibility: 'If the course followed by the United Kingdom resulted in a confrontation with the Commission this would heighten the risk of a substantial disallowance' (EQO(83)39, 29 June 1983).

5. As to how best to proceed with the Commission, I am sure the key, as you say, is to indicate our willingness to do a deal under

/which

which the MMB's objectionable practices would be reformed and the disallowance issue would be dropped. I think we need to begin discussions with them without delay. I noted from the record of your recent meeting with Christopher Tugendhat that you said you were not prepared to enter into a negotiation with DG V1 over possible changes by the MMB. I can see that it may have been necessary to take this line in advance of Ministerial consideration here but now that we have cleared our lines we should surely tell him promptly that we are accepting his advice. That should encourage him to deal expeditiously and helpfully with the 1978 and 1979 disallowance cases and as slowly as possible with the later years.

6. I am copying this minute to members of E(A), the Attorney-General and the Secretary to the Cabinet.

GEOFFREY HOWE
Foreign and Commonwealth Office
20 January, 1984

Agriculture : Milk Prices
Pt 2

10 DOWNING STREET

Prime Minister

Both Policy Unit and Cabinet Office oppose any increase in liquid milk prices

(i) farmers are still over-producing

(ii) distributors do not need an increase yet.

In addition to resisting a price increase, you should seek maximum involvement of DTI and Treasury in reviews of

(i) statutory price controls

(ii) future of MMB's.

AT

18/1

cc Mr Redwood

MR. TURNBULL

LIQUID MILK PRICES

We question the case for increasing milk prices. Although the traditional costings exercises point in this direction, wider considerations - CAP reform and our negotiating position on it, and the need for more competitive arrangements in milk production and distribution - argue for a break with this price-fixing tradition, as a prelude to a fundamental change in the milk sector.

How Badly Off is the Dairy Farmer?

1983/84 has been a poor year for the dairy farmer. A wet Spring reduced yields and raised feeding costs. The estimates shown in Appendix 1 of Mr Jopling's paper suggest that, following an excellent year in 1982/3, the net margin per cow is lower in real terms this year than it has been in the previous poor years (1976/77, 1980/81 and 1981/82).

This trend is of no particular relevance. What matters to any business is whether or not it is profitable. MAFF's own survey data suggests that the average dairy farmer, with 68 cows, will make a net profit on his dairy business this year of £5,800 (68 x £86), after allowance for all costs, including the farmer's own pay, and imputed rent on land, but not interest. There are also the proceeds from other activities on the typical farm. 1981/82 survey data suggested that these add another 40% or more to net profit, bringing it up to £8,200. The typical farmer in the survey has assets worth around £120,000, excluding land, in respect to which a rent is imputed. He therefore earns a return on his assets of 7%, in addition to his attributed wages (and other benefits from living on a farm often chargeable as business expenses).

This may explain why the dairy industry has not as yet responded to this decline in margins. The cow population is increasing slightly and the market price of in-milk heifers (£856 in December 1983) was only 6% down on a year earlier.

A decline over time of net margin per cow is probably to be expected. Average herd size is increasing by around 3% a year. Over time, farmers could survive on lower margins per cow, by spreading overheads over larger herds.

Changes Facing the Milk Sector

The marketing and pricing arrangements which have suited the industry for over 50 years in some cases are becoming increasingly less appropriate:

i. the stabilisation of the dairy farmers' income has been taken over (for better for worse) by the CAP;

ii. the stabilisation of farm incomes cannot be pursued regardless of demand, and efficiency, when the rest of the economy is having to make major adjustments;

iii. the cosy arrangements to maintain dairies' margins will break down in the face of competition from imports and are, in any case, difficult to reconcile with our approach to competition generally.

Mr Jopling argues that one should not terminate the arrangements, nor suspend their operation while price controls are in place, because this would deprive the industry of the advantages of the system without giving them the benefits of a free market. We agree that the price control arrangements cannot be terminated now, not because of "uncertainty", but because the MMB, with its statutory monopoly, is too powerful to be left unchecked.

It does not follow from this that the present system need be suspended. Mr Jopling could announce that he has decided not to raise wholesale prices because he had also to have regard to the industry's operating context. This must include wider considerations than maintenance of farm incomes and distributors' margins, for example, budgetary implications and the industry's need to respond more competitively to the threat from imports.

The following points are relevant:

i. the demand for liquid milk is declining at 1-1½% a year;

ii. supermarkets are expanding their market share, doubling it to 16% over the last four years, by setting prices at (at least) 2p per pint lower than the doorstep price;

iii. imported UHT milk has made little inroads as yet, but the recent French consignments were no more than tests of the new legislation. UHT could take a growing market share because its taste is improving. Efficient continental cooperatives might get it into UK supermarkets at 15p per pint, or even less; and the growing milk surplus in the Community will be looking for any outlet which is more profitable than intervention.

Since the marketing arguments all point towards price restraint for liquid milk, a decision to allow price increases would encourage the industry to move in precisely the wrong direction.

The dairies have not yet come to terms with these changes; they benefit from the cost-plus Binder-Hamlyn arrangments which in effect set a common price throughout the country; they have established restrictive agreements, they have not deployed much marketing flair in adding other products to the milk round.

The Review of Present Arrangements

Mr Jopling's review of pricing arrangements needs to go much wider than pricing and should involve Departments other than his own. The existence and behaviour of the MMB itself must be considered. By offering farmers a uniform "pooled" price, irrespective of their location, the MMB encourages and perpetuates a geographical pattern of dairy farming which is ineffecient. Its licensing policy towards farmers who might wish to develop into processing and retailing needs a review. Its discriminatory pricing policies (eg charging 3p per pint more for raw milk retailed as liquid milk than for raw milk used for processing) must damage milk users and it requires a large staff to police.

Conclusions

Although precedent encourages the industry to expect price increases, based on costings surveys, wider considerations argue against price increases at either the retail or the wholesale level.

1. Dairy farmers' margins are probably historically low, but they do not seem to be disastrous for the average farmer. In any case,

/income support

income support can no longer be the overriding consideration, given our support for draconian measures to curb CAP excesses (nominal price reductions, the super-levy).

2. Milk distributors' paramount need is to adopt a more competitive approach, in order to counter the potential threat from imports and the decline in milk consumption. (It might be difficult in any case to allow an increase for them and not for the farmer.)

4. The review of milk marketing must be widened to include the future of the MMB. After consultation with Mr Lawson and Mr Tebbit (and their officials), Mr Jopling should be asked to bring his review back for collective discussion.

NICHOLAS OWEN
18 January 1984

CONFIDENTIAL

P.01206

PRIME MINISTER

Liquid Milk Prices in England, Wales and Northern Ireland

Flag A (E(A)(84)2)

BACKGROUND

In England, Wales and Northern Ireland the Government controls the maximum price of milk sold for consumption in liquid form. Maxima are set both for the price charged by the Milk Marketing Boards (MMBs) to the distributors and for the price of retail sales. The controls, which derive from war time arrangements for regulating prices and distributive margins for essential foodstuffs, have been retained by successive governments largely on the grounds that because the MMBs are monopoly suppliers, there are relatively few large distributors, and there has been no effective competition from imports, the consumer has to be protected from exploitation. Because maximum prices largely coincide with actual prices, they effectively determine the margin received by distributors. This margin is the subject of arrangements established in 1982 following recommendations by the accountants Binder Hamlyn and lengthy negotiations with the dairy trade. Further details of the system are given in Annex A to this brief.

2. The Scottish system diverged from the rest of the country in 1981; and since 1 January 1984 there has been no control over milk prices in Scotland. The difference is supposed to reflect differences in Scottish circumstances, notably in the system of milk distribution.

3. Towards the end of last year, there was Ministerial correspondence following proposals from the Minister of Agriculture, Fisheries and Food for increases in the maximum retail and wholesale prices of liquid milk. The letter of 20 December from the Chancellor of the Exchequer argued against any increase in the retail price, on the grounds that it would not be consistent with our aim of reducing the production of milk, which is in chronic over-supply in the European Community. He also questioned the justification for controlling milk prices at all. Your Private Secretary's letter of 21 December supported these points, and said that if Mr Jopling wished to pursue his proposals he should bring them forward for collective discussion.

Flag B

Flag C

4. This Mr Jopling has done in his memorandum E(A)(84)2. He proposes that the maximum retail price of liquid milk should be increased by 1p a pint from 4 March, 1984, and the maximum wholesale price by 0.91p a litre from 1 February 1984; there would be an increase in the dairy trade's target rate of profit under the 'Binder Hamlyn' arrangements. The effect would be to split the proceeds of the increase in the maximum retail price about equally between producers and distributors. Mr Jopling agrees with the Chancellor of the Exchequer that the justification for price controls needs to be examined, and says that he has set up a departmental review to that end, but argues that the present arrangements should not be terminated immediately. He does not agree that an increase in milk prices would be inconsistent with our aim of restricting milk production in the Community. He argues that it would be wrong to discriminate between producers in the various Member States; that it would be wrong to put our producers at a disadvantage; that to do so would not strengthen our negotiating position in Brussels; and that it would have serious effects on the industry. ? Scotland?

MAIN ISSUES

5. The main issues before the Sub-Committee are as follows.

(i) Should the present system of controls over milk prices be scrapped immediately?

(ii) If the system is to be retained, at least for the time being, should Mr Jopling's particular proposals be accepted?

Scrap the system forthwith?

6. Some members of the Sub-Committee may suggest that the system should be scrapped immediately, for the following reasons.

(a) Price control is clearly incompatible with the Government's general economic philosophy.

(b) The main justification for the existing system is to protect the consumer against exploitation in the absence of effective competition from imports. But we are now admitting imports of UHT and sterilised milk; and they should provide the necessary competition.

(c) Scotland is apparently able to manage well enough without price controls. Against this, it is argued that Scottish circumstances are different: in particular, the system of door-step delivery of milk is much less important in Scotland than elsewhere (it accounts for only about half of total sales, compared with about 90 per cent in England and Wales); and it is the system of door-step delivery which is said to be particularly vulnerable to changes in the existing arrangements. But the arguments are far from clear-cut.

7. We understand that Mr Jopling is likely to reply that he does not necessarily dissent in principle from these points (indeed, that is why he has set up a review); but that it would be dangerous to move too quickly for the following reasons:

(a) Imports do not yet offer effective competition (and it is arguable that we do not want them to do so).

(b) It would be difficult to scrap the system of control over retail prices without also scrapping control over wholesale prices: otherwise, distributors would appear to have a licence to exploit the consumer. But scrapping control over wholesale prices could call into question the role of the MMBs. It may be right to do this; but the implications are complex and require careful study.

(c) There would be much public disquiet about the possible effects on doorstep deliveries. The Government needs to have studied all the implications of de-control, so that it can deal with such disquiet effectively.

The present proposals

8. Even if the Sub-Committee agree that it would be wrong to scrap the present system immediately, several Ministers are likely to argue that it would be wrong to increase the maximum retail price now. The following points need to be considered:

(i) the effect on the farmers;

(ii) the effect on the distributors and thus on doorstep deliveries;

(iii) the effect on negotiations in the Community.

Effect on farmers

9. Mr Jopling argues (para 1 of Annex A to E(A)(84)2) that the milk producers, who had a good year in 1982, had a bad year in 1983 and are worried about the impact of EC milk "super levy"; and that their income should therefore be increased. Other Ministers may argue that this is hard to justify when milk is in such over production throughout the Community. Moreover it is not clear that UK milk producers are far out of line with those elsewhere in the Community. The average price received by UK producers for milk in 1981 (the latest available figures) was 94 per cent of the Community target price, compared with 89 per cent in Ireland, 93 per cent in Germany, 97 per cent in France and 101 per cent in Denmark.

Effect on distributors

10. Much of the political concern in the past has been about maintaining doorstep deliveries. The element in the present arrangements most relevant to that would appear to be the distributors' margin. Under the Binder Hamlyn arrangement there would appear to be a case for increasing the margin by just under 1p per litre, ie about ½p per pint. If Ministers wished to keep the maximum retail price steady but increase the distributors' margin, there would have to be a reduction in the maximum wholesale price of ½p, thus actually worsening rather than improving the position of the farmers. But it is not clear that such an increase in the margin would be justified immediately. The figures in Appendix II to E(A)(84)2 suggest that at 31 March 1984 the distributors will have been cumulatively overpaid by £25 million. It seems likely that during the summer they will move into a position of cumulative underpayment but even by 30 September 1984 the cumulative underpayment is expected to be under £10 million. Any increase in the distributors' margin and any increase in the maximum retail price arising solely from that might therefore possibly be deferred until the late summer or autumn.

Effects on negotiations in the Community

11. Both you and the Foreign Secretary have pointed out the inconsistency of arguing in the Community for a reduction in milk prices, while increasing domestic prices. Mr Jopling replies that a price freeze would not strengthen our negotiating position.

?

12. A related but separate point is the extent to which penalising domestic producers could make it more difficult to secure their acceptance of reforms in the CAP, as Mr Jopling argues. On the other hand, there are obvious objections to accepting that the possibility of changes in the CAP, uncertain as to both their timing and their nature, should be a bar indefinitely to changes in our domestic arrangements. It is explained in paragraph 12 of the Annex to this brief that the difficulties which have recently arisen with the Commission over "disallowance" relate to milk for manufacturing rather than liquid milk and ought not to make it more difficult for the Government to take a hard line with UK dairy farmers and the trade, should this be justified.

A possible way forward

13. If the Sub-Committee were to feel that it would be undesirable to scrap the present system of price control without waiting for the outcome of the review Mr Jopling has set in hand, a way forward might be to defer any action until later in the year. As explained above the case for increasing the income of the farmers at a time of excessive overproduction is questionable. Even if the case for an increase in the distributors' margin is accepted, it is not clear that such an increase would be required until the late summer or early autumn. By then the dangers of an adverse effect on our negotiating position in the Community might be less. The greatest advantage would however be that Ministers might then be in a position to decide whether or not to keep the present system of price controls for liquid milk.

Arrangements for policy reviews

14. The review of the liquid milk price control arrangements and the review of the future rôle of the Milk Marketing Boards arising out of the problems with the Commission on milk for manufacturing (see paragraph 12 of the Annex to this brief) are separate from the review of UK domestic expenditure on agriculture, led by the Cabinet Office, which was agreed at your meeting with Mr Jopling before Christmas. The existence of this expenditure review is not known outside the Treasury and the agricultural departments and you will not wish to refer to it at E(A). We shall however make sure that there is appropriate liaison between progress on the two reviews of the milk arrangements and that on the expenditure review.

Announcements

15. If the Sub-Committee were to approve Mr Jopling's proposals he would wish to announce them, following the usual practice, by written Question and Answer as proposed in Annex B to E(A)(84)2. It may be convenient to ask him to clear the text in correspondence rather than deal with it at the meeting.

HANDLING

16. You will wish to invite the Minister of Agriculture, Fisheries and Food to introduce his memorandum. The Secretaries of State for Northern Ireland and Wales could add any points affecting their countries. The Secretary of State for Scotland may be able to comment on the implications of de-control, at least in Scottish circumstances. The Chancellor of the Exchequer could then be invited to reply. The Foreign and Commonwealth Secretary will have comments from the standpoint of negotiations in the Community.

CONCLUSIONS

17. You will wish the Sub-Committee to reach conclusions on the following.

(i) Should the present system of control of maximum retail and wholesale prices of liquid milk be retained, at least pending the outcome of the review which Mr Jopling has put in hand?

(ii) If so,

a. should there be an increase in the maximum retail price by 1p a pint, together with increases in the maximum wholesale price and dairy trade's margin as proposed in E(A)(84)2, or

b. should any increases be postponed until later in the year when the review of price control arrangements has been completed?

(iii) The timing and content of any announcements.

PLG

P L GREGSON

18 January 1984

ANNEX

Milk Pricing Arrangements

About half the milk produced in the UK is used for manufacturing milk products, and about half for consumption as liquid milk. The pricing arrangements for the two sectors differ.

2. In the manufacturing sector the Milk Marketing Boards (MMBs) negotiate prices directly with producers. The prices for milk used for different products broadly reflect the prices which the products will realise. Manufacturing milk prices are therefore determined essentially by the markets for milk products; these are underpinned by the intervention prices set by the Community for butter and skimmed milk powder.

3. For liquid milk the Government sets, in England, Wales and Northern Ireland, maximum wholesale and retail prices to reflect its judgement of what the market will bear; what margins should be given to processors and distributors; and what level of returns milk producers should receive. Although these prices are technically maxima, they generally coincide with the actual price: the only significant exception is that some super markets sell milk below the maximum retail price.

4. Since 1 January 1984, there has been no system of control of milk prices in Scotland.

5. Milk sold for consumption as a liquid commands a premium of about 20 to 25 per cent over milk sold for manufacturing. However, the MMBs pool what they realise from both sectors and pay producers a common 'pool' price, irrespective of the use to which their milk is put.

6. The controls over the maximum price of liquid milk derive from wartime arrangements. They have been retained by successive Governments, largely on the grounds that:

(a) the MMBs are monopoly sellers;

(b) there are only a few relatively large milk distributors; and

(c) that in the absence of liquid milk imports the Government must establish maximum prices at which the MMBs and distributors can sell their products in order to protect the consumer from exploitation.

7. Ministers agreed in March, 1981 to retain controls over the price of liquid milk (E(81)11th Meeting).

8. The control of distributors' margins inherent in the system of price control is based on recommendations by the accountants Binder Hamlyn. Basic target rates of profit are established:

(a) for the processing plants of the dairying industry by comparison with the rate of return on capital in a reference group of food manufacturers;

(b) for the retail part of the industry by comparison with the rate of profit on turnover in a specified group of food retailers.

Community implications

9. Milk is in chronic over-supply in the European Community. Production is 20 to 25 per cent higher than consumption, and

growing at 2 to 3 per cent a year, whereas consumption is stagnant. Disposing of the resulting surpluses requires heavy subsidies. Milk accounts for about 30 per cent of expenditure on the CAP.

10. Although the UK's system of controlling liquid milk prices is largely independent of the CAP (our current dispute with the Commission about milk prices, and the possible disallowance of certain items of agricultural expenditure, relate to milk sold to manufacturing), increasing the price paid by consumers and the price paid to producers will tend to reduce consumption and encourage production. As a result, more milk will be offered for manufacturing and will ultimately have to be bought by the Intervention Board for Agricultural Produce (IBAP). The cost in 1984-85 is estimated at £20 million, which will fall in the first instance on the Exchequer. Most, but not necessarily all, the cost will be recovered when the products held by IBAP are sold.

11. Much discussion is taking place in the Community of possible methods of limiting milk production. The likely outcome of these discussions is still far from clear.

12. The "disallowance" issue with the Commission which, as explained above, relates to milk for manufacturing rather than to liquid milk, ought not to have any significant bearing on the decisions Ministers take about liquid milk. The Minister of Agriculture has proposed (his minute of 13

Flag D

January) and the Chancellor of the Exchequer has agreed (his

Flag E

minute of 17 January) that the MMBs should be persuaded, or in the last resort compelled, to stop the pricing practices to which the Commission has objected. Although the MMBs are likely to claim that it will be commercially disadvantageous to them to make these changes, there is no evidence as yet that there would be any signicant harm either for the dairy trade or for farmers. The problem which has arisen in this area ought not therefore to be an argument against doing whatever Ministers think desirable on liquid milk. The point at which the two issues come together is in the review of future milk marketing arrangements. The Minister of Agriculture has already agreed to review the statutory price controls for liquid milk. He has also separately agreed, in the context of milk for manufacturing, to review the present organisation and powers of MMBs. In that latter context the Chancellor has suggested that the review should cover the possibility of the abolition of the MMBs. Major and fundamental changes might therefore result from the combined effect of these two reviews.

CONFIDENTIAL

cc NO

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

Prime Minister.

Do you wish to consider in E(A) on Thursday whether and how to conduct a fundamental review of the Milk Marketing Board, as the Chancellor suggests?

A.J.C. 18/1

PRIME MINISTER

MILK MARKETING ARRANGEMENTS AND THE THREATENED FEOGA DISALLOWANCE

The Minister of Agriculture sent me a copy of his minute of 13 January.

2. I agree with Michael Jopling that we must take urgent steps to minimise the risks of disallowance over the years since 1978 and to remove the possibility of building up further risks in future. Even if the threat of disallowance of 1978 and 1979 expenditure is averted, the sums potentially at risk for subsequent years are extremely large: the Intervention Board for Agricultural Produce has spent over £1 billion since 1980 in supporting the milk market.

3. We shall need to consider carefully, in the light of the Foreign and Commonwealth Secretary's advice, how best to proceed with the Commission in respect of disallowance of 1978 and 1979, on which, as Michael reports, there is a difference of opinion within the Commission.

4. As to how we should proceed in respect of the later years, I agree with Michael Jopling that:

a. urgent discussions should be held with the milk industry to seek to persuade them to discontinue the pricing arrangements to which the Commission object;

CONFIDENTIAL

b. we should be ready to legislate if the industry are unwilling to make these changes voluntarily;

c. on that basis we should seek to do a deal with the Commission to avoid the infraction proceedings and the risk of disallowance for 1980 onwards;

d. we should take a fundamental look at the present organisation of the Milk Marketing Boards and the powers they exercise.

5. I regard the last point as of particular importance. Clearly, avoiding the threat of disallowance must be our immediate priority; but we must also consider whether we should continue to maintain any special arrangements, statutory or otherwise, for the organisation of the milk markets. The present complex of statutory controls and customary restrictions is quite at variance with the general thrust of our economic policies. So we need a fundamental review of the arrangements in which all options, including the abolition of the MMBs, are kept open; and we should avoid any suggestion that if the Boards drop the pricing practices to which the Commission has objected, the present system will continue in more or less its present form. You may wish to consider further in E(A), on Thursday, how and when such a review might proceed: the decisions about milk prices which we have to take at that meeting are of course another illustration of the difficulties to which market regulation gives rise.

6. I am sending copies of this minute to members of E(A), the Foreign and Commonwealth Secretary, the Attorney General and the Secretary to the Cabinet.

NL.

(N.L.)
17 January 1984

EURO POL
CAP
Pt 12

17 JAN 1984

FILE 8H

10 DOWNING STREET

From the Private Secretary

16 January, 1984

Milk Marketing Arrangements and Threatened FEOGA Disallowance

The Prime Minister saw over the weekend your Minister's minute of 13 January on the above subject and has noted its contents.

I am copying this letter to Roger Bone (Foreign and Commonwealth Office), John Kerr (H.M. Treasury), John Lyon (Northern Ireland Office), the Private Secretaries to the Secretaries of State for Scotland and Wales and to the Attorney General and Richard Hatfield (Cabinet Office).

A.J. COLES

R. Lowson, Esq.,
Ministry of Agriculture, Fisheries and Food

cc NQ

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

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NL.

(N.L.)
17 January 1984

PRIME MINISTER

MILK MARKETING ARRANGEMENTS

Please see the attached minute from Mr. Jopling.

This is potentially a very troublesome subject. You will see that the Commission have long objected to the differentiated selling prices used by the Milk Marketing Boards. They are now threatening to disallow expenditure on milk in the UK for 1978 and 1979 - which could amount to £463m. Worse, they might also disallow expenditure for 1980 to 1983 which, at the extreme, could amount to £1b.

David Williamson tells me that:

a) It is difficult to defend the Milk Marketing Boards' practices with regard to selling prices;

b) He agrees with the action that Mr. Jopling now proposes to take.

A.J.C.

13 January 1984

cc NO

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

CONFIDENTIAL

PRIME MINISTER

13 January 1984

MILK MARKETING ARRANGEMENTS AND THREATENED FEOGA DISALLOWANCE

You will wish to know that we are now confronted with some very difficult issues related to our domestic milk marketing system. I am minuting you immediately because the sums of money involved are very large and would be directly relevant to the negotiation on the budget problem; and because of the substantial domestic political repercussions in relation to our regime for marketing milk through the statutory Milk Marketing Boards (MMBs).

The background in brief is that the Commission and other Member States have always harboured suspicions of the MMBs, and in particular as incompatible with a common organisation of the market under the CAP. In 1978 and 1979, we negotiated regulations which authorised the continued operation of the MMBs subject to certain constraints on their freedom in pricing milk in negotiation with the dairy trade in the United Kingdom. It is these milk pricing arrangements which have continued to cause the trouble.

The Commission have argued that certain of the practices under which the MMBs and the dairy trade have agreed to differentiate the selling prices for milk for different end uses are contrary to the provisions of the relevant regulation. On butter, they have objected to separate selling prices for milk for bulk (mainly intervention) butter and packet butter. On skim, they have objected to the three price structure under which there is a lower price for manufacture into skimmed milk powder, and two higher prices for liquid skim for stockfeed and for high value products like yoghurt. In addition, they have taken issue with arrangements under which preferential prices are charged for milk for certain products for export to third countries which they argue is tantamount to an additional export subsidy.

/There have

There have been detailed discussions with the Commission over the last five years to try to establish a clear understanding about what types of prices differentiation are permissable under Community law. But it has not been possible to reach any clear conclusions about what sort of price differentiation the Commission would find acceptable. At the same time, we have had detailed discussions with our industry during which we have pressed them to give up multiple pricing. But they have argued strongly that their present practices are essential to maintain their competitive position in the UK and export markets and that they are doing nothing different in principle to what the continental co-ops in France and the Netherlands do in differentiating their product selling prices according to competitive needs in different markets. They recently agreed to drop dual pricing of butter, though the implementation of this decision awaits the outcome of arbitration on how it should be done. But the industry have been unwilling to move on skim or exports without a Court ruling against us. The legal advice has always been that the Government has no powers to force the industry to change their pricing arrangements unless and until there is a clear Community obligation to do so as a result of an adverse Court finding.

Encouraged by the Irish who are out to weaken our marketing arrangements so that they can compete more effectively for a bigger share of our markets, the Commission decided last year to initiate infraction proceedings against us on butter and skim milk, and they have more recently taken the first steps also on export pricing. The legal process will lead to a European Court hearing probably towards the end of this year unless the progress of the cases is in some way aborted. The Law Officers have advised that our case on butter is weak; but that we may be on stronger grounds in defending infraction proceedings on skim and export pricing. The Irish Dairy Board have initiated legal proceedings in the High Court against the MMB seeking compensation for trading losses which they claim to have suffered on account of dual pricing of butter.

Quite separately from these infraction proceedings, a new and more urgent issue has now arisen. There is a risk that the Commission could decide to disallow expenditure on milk in the UK when they come to clear the FEOGA accounts for the years in question. We were first warned of this possibility last year, though the Commission did not give any indication of the expenditure which they would regard as relevant or the nature of the case they would argue. This issue could arise on the 1978 and 1979 accounts which are due to come to the Commission for clearance within the next few weeks. We were told last August that DG VI would not propose disallowance for these years because the regulations governing the MMBs activities within the Community were not implemented until the middle of 1979. But at a meeting in the middle of December, it emerged that DG XX (the Financial Controller) was recommending disallowance of all milk expenditure in the UK for these two years. If the Commission were to adopt this recommendation, the sums in question, on our figures, could amount to £463 million.

/Although ...

Although a disallowance on this scale would seem virtually unthinkable, it would clearly cause us great political difficulty if the Commission were to decide on any substantial disallowance for 1978 and 1979 in the next few weeks whatever the ultimate outcome might be. Since the Commission could begin to clawback immediately the monies involved by reducing the allocations to IBAP pending the Court's decision, there would clearly be substantial implications for our budget negotiations, which outside commentators would be quick to see.

Intervention board

Although there is disagreement between DG VI and DG XX on the appropriate course of action in relation to 1978 and 1979, we understand that all parts of the Commission agree that the relevant expenditure should be disallowed in 1980 and later years. Again there remains uncertainty about the extent of the disallowance which the Commission might decide. The sums involved in 1980 to 1983 inclusive could be very substantial, and since the industry is still operating the practices complained of, we shall continue to build up additional risks in 1984 unless the present practices are stopped.

up to £1 billion, I understand. A.J.C. 13/1

I should make it clear that it would be quite unprecedented for the Commission to disallow the whole of the expenditure in a particular commodity sector, and on the scale being recommended by DG XX. The Law Officers take the view on disallowance that the European Court would support the Commission in going beyond the existing precedents, but not in claiming that all expenditure should be disallowed. They consider that it would be necessary to show, not only that the practice complained of was illegal, but also that there had been an increase in FEOGA expenditure as a result. It is clear, however, that we are faced now with very substantial financial risks that could not previously have been foreseen; and that we must now take urgent steps not only to seek to minimise the risks of disallowance over the years since 1978; but also to remove the possibility of building up further risks in future.

Following full discussion of these issues at official level between the Departments concerned, I am proceeding immediately as follows:-

a) I have spoken myself this week to Messrs Tugendhat and Dalsager on the disallowance issue, particularly in relation to the clearance of the accounts for 1978 and 1979. Officials have also had discussions with DG XX.

As I have said, these two accounts are due to come to the Commission soon and we must keep up the pressure to avoid a decision by the Commission to disallow in this context. It is clearly very important to try to avoid an issue over disallowance emerging at this stage.

b) I shall be having urgent discussions with the milk industry to seek to persuade them to discontinue the pricing arrangement complained of. Given the importance which the industry attach

/to multiple ...

to multiple pricing in maintaining their competitive position particularly on exports, we have a politically difficult problem on our hands in getting them to change their practices voluntarily. If necessary, I shall have to be ready to indicate that the Government would be prepared to legislate urgently if the industry are unwilling to make the changes voluntarily. Whatever form such legislation took, it would be bound to be highly controversial.

c) On the basis of (b), I should seek to do a deal with the Commission to avoid both the infraction proceedings and the disallowances being pursued. We should put it to the Commission that, since the pricing practices complained of were to be ended, the infraction proceedings were not necessary. It is impossible to judge how far the Commission would be prepared to commit themselves in a deal of this sort. We should need, therefore, to maintain our view that no breach of Community law has been committed so that we do not weaken our position if it should still become necessary either to defend infraction cases or to oppose disallowances.

d) Work is already in hand on the amendments that might be made to our present milk marketing arrangements in order to avoid in future continuing scope for challenge by the Commission and other Member States. This means taking a fundamental look at the present organisation of the Milk Marketing Boards and the powers they exercise. You will understand that this is highly sensitive territory because of the fundamental role of the MMBs to our whole milk sector, andthe current concerns about damage to the doorstep delivery system from cheap imports. We shall need to feel our way forward with the powerful interests concerned and not least our supporters in Parliament. But I am clear that we must find ways of avoiding in the future continuing problems with the Community over our milk set-up. I shall put my proposals to colleagues on all of this just as soon as possible.

I should add that we must avoid if possible public discussion of the threat of disallowance on the 1978 and 1979 accounts. It is clear that, if there is any suggestion that we are putting political pressure on the Commission not to disallow, this could be highly counter productive when the issue comes before the Commission.

I am sending copies of this minute to the Foreign and Commonwealth Secretary, the Chancellor, the Secretaries of State for Northern Ireland, Scotland and Wales, the Attorney General and the Secretary to the Cabinet.

MJ

MICHAEL JOPLING

ICCNO

DEPARTMENT OF TRADE AND INDUSTRY
1-19 VICTORIA STREET
LONDON SW1H 0ET
Telephone (Direct dialling) 01-215) 5422
GTN 215)
(Switchboard) 215 7877

JU372A
Secretary of State for Trade and Industry

11 January 1984

The Rt Hon Michael Jopling MP
Minister of Agriculture, Fisheries & Food
Ministry of Agriculture, Fisheries & Food
Whitehall Place
London SW1

Prime Minister
To note. A paper on this will come to E(A) next week
AT 11/1

Dear Minister,

LIQUID MILK PRICES

I have seen copies of the correspondence resting with Geoffrey Howe's minute to you of 29 December.

2 I strongly support the view that we should examine very carefully whether the existing system of control over liquid milk pricing, and the Milk Marketing Board's monopoly, is any longer right or necessary. Milk is a sector in which, on the face of it, our system of regulation is plainly at odds with our wider policy of achieving economic efficiency through competition and the mechanism of free market forces. What is more, there is evidence that it has provided a sheltered environment within which restrictive agreements between the dairies have flourished. Some seventy of these have recently been uncovered by the Director General of Fair Trading, who will be taking them before the Restrictive Practices Court. I understand that they involve most of the major dairies, cover different parts of the country, and provide for restrictions of competition in such fields as pricing and tendering for milk supplies to local authorities and hospitals. Against this background, and while acknowledging the popularity of the doorstep delivery system, I think it essential for us to have a searching look at the merits of our system of regulation, before conceding the need for any milk price increase.

3 More generally, the trend in the retail price of fresh milk compared with food retail prices as a whole seems to me to underline very clearly the impressive - and depressing - lesson of uncompetitive pricing in an over-regulated and over-subsidised sector. Over the ten years since January 1974, the retail price of fresh milk has risen by 278.4 per cent, compared with a rise of 214.5 per cent for food generally; and although the differential is less marked in the last five years, it has

ccNO

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JU372A
Secretary of State for Trade and Industry

11 January 1984

The Rt Hon Michael Jopling MP
Minister of Agriculture, Fisheries & Food
Ministry of Agriculture, Fisheries & Food
Whitehall Place
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remained, with fresh milk retail prices rising by 56.6 per cent, compared with 51.3 per cent for food generally. These figures speak for themselves. I see the regular need to increase milk prices as a clear consequence of the continuing subsidy to producers.

4 I am sending copies of this letter to the Prime Minister, Nigel Lawson, Geoffrey Howe, George Younger, Jim Prior, Nicholas Edwards and Sir Robert Armstrong.

Yours sincerely

M McCarthy
(approved by the Secretary of State, and signed in his absence)

NORMAN TEBBIT

Agric Milk pt 2

11 JAN 1984

cc NO

Prime Minister

To note. This accords with your views, which we have already conveyed to the Minister for Agriculture.

DWS 30/12

FCS/83/279

MINISTER FOR AGRICULTURE, FISHERIES AND FOOD

Liquid Milk Prices

1. Nigel Lawson sent me a copy of his letter of you of 20 December on milk. I have also now seen your letter to him of 6 December.

2. It would be difficult to justify putting up the price of milk - already among the most expensive in the Community - at a time when we are arguing in Europe for large price reductions or, failing that, an extended price freeze. To do so would be bound to weaken our negotiating position. I therefore support the Chancellor's opposition to this proposal.

3. I agree with Nigel Lawson, too, that it is time we looked hard at the whole complex of controls over liquid milk. There may indeed be a case for going further and considering the future of the Milk Marketing Boards. As I said to you in my letter of 22 July about the Commission's cases against us on multiple pricing, our operation of a milk marketing monopoly has always caused and will continue to cause us trouble within the Community. Many of our colleagues in the Party are also philosophically hostile, and you may have seen an article in the Economist recently which suggested ending the milk marketing monopoly. There is at least a case for an investigation by the Monopolies Commission. If we did decide to take action on this front it would certainly fit in well with our general European policy.

/4. I am

4. I am sending copies of this minute to the recipients of your letter, and to Norman Tebbit.

GEOFFREY HOWE

Foreign and Commonwealth Office
29 December 1983

Agriculture: Milk Prices Pt 2

RESTRICTED

SC NO.

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
Treasury Chambers
Parliament Street
LONDON SW1P 3AG

23 December 1983

Prime Minister (2)
To note that milk prices will have to be considered collectively.
DRB 30/12

Dear Nigel

LIQUID MILK PRICES

Thank you for your letter of 20 December about the proposals for milk price changes set out in my letter of 6 December.

I cannot accept your suggestion that the changes I have proposed would be inconsistent with agreed objectives of agricultural policy. In particular my proposals take full account of the needs of the consumer: this would be the first retail price increase for nearly 16 months, which is much longer than usual, and the increase would be 1p a pint rather than the 1½p a pint that would have been in line with the trend of previous price increases. I am also proposing that we should freeze the price at its new level for a further year partly for the benefit of the consumer and partly to provide a period of stability for the industry during which we can give thorough consideration to the arrangements that should apply from Spring 1985 onwards. As regards producers, the award would be modest, particularly given the very substantial decline in net margins which they are currently experiencing.

I shall be putting a paper to colleagues early in the New Year with a view to resolving the matter in time for the increase in the producer price to take place from 1 February instead of 1 January as I originally hoped.

I am sending copies of this letter to recipients of my original letter, and to Geoffrey Howe and Norman Tebbit.

Yours ever
Michael

MICHAEL JOPLING

RESTRICTED

Agriculture, milk prices, pt 2

30 DEC 1983

JR LPO

[illegible]

10 DOWNING STREET

From the Private Secretary

21 December 1983

Dear Ivor,

The Prime Minister has seen your Minister's letter of 6 December to the Chancellor and the replies from the Chancellor and the Secretary of State for Northern Ireland. With milk in substantial surplus, she would prefer to avoid any increase in the retail price. This would be more consistent with the line taken at Athens where the UK argued for a three-year freeze on the intervention price for milk. If your Minister wishes to pursue this proposal it should be brought forward for collective discussion.

The Prime Minister agrees with the Chancellor that the statement ought to go further in indicating the possibility that the system of statutory controls over milk prices might be substantially reviewed and possibly abolished altogether. She therefore agrees with a re-draft along the lines suggested by the Chancellor.

I am sending copies of this letter to the Private Secretaries to the Chancellor of the Exchequer, the Secretaries of State for Scotland, Northern Ireland and Wales, the Foreign and Commonwealth Secretary, and the Secretary of State for Trade and Industry and to Richard Hatfield (Cabinet Office).

Yours sincerely

Andrew Turnbull

ANDREW TURNBULL

Ivor Llewelyn, Esq.,
Ministry of Agriculture, Fisheries and Food.

JC

1

File

Agriculture: ~~Europe~~

10 DOWNING STREET

Prime Minister

Agree

(i) no increase in the retail price of milk

(ii) greater indication of changes to come, as suggested by Chancellor and PU?

AT 20/12

We spoke about this

1) In view of the Chancellor's look at milk where we urged a 3 year freeze with MAFF support I do not think there should be any milk increase this coming year.

2) - as (ii) above - agreed not

PRIME MINISTER

LIQUID MILK PRICES

The arrangements for pricing and distributing milk are bizarrely different from those applying to any other industry; they involve uniform farm gate prices, unrelated to transport costs; monopoly boards, a distributors' cartel with assured profit margins. It is no surprise that milk is expensive in this country.

The case for dismantling this system is made stronger by three considerations:

i. our approach to competition policy (and indeed, to economic policy generally) which the Policy Unit has suggested should be developed with emphasis on major items of the household budget - housing, travel and food;

ii. the overriding need to reduce the community milk surplus, by drastic means if necessary (freeze on intervention prices, a super levy). We shall soon be in surplus ourselves, but in any case, we are part of the Community market: additional UK milk has contributed to the CAP's financial problems;

iii. the admission of imported milk.

It is important that the statement prepares the industry for these changes. As drafted, it conveys exactly the opposite impression: that the Government will see the industry right, in cosy discussions with "the interests concerned", without even mentioning the CAP. Whether a price increase is granted or not, we think that the penultimate paragraph might be redrafted as follows, taking in the Chancellor's suggestion:

"I do not intend to make further changes to these maximum milk prices until the early part of 1985. I have taken a longer perspective than usual in making these price determinations [or: "this decision"] because I am aware of the impending changes in the circumstances of the dairy industry, arising from the admission of imports and the need to take important

/decisions

decisions about the future of the CAP. I shall be reviewing the position thoroughly next summer and autumn with a view to deciding on whether and if so in what form statutory controls over milk prices should apply from the spring of 1985."

The Chancellor does not agree to any increase in the retail milk price. Since it was part of our negotiating position in Athens that the levy should be accompanied by a three-year freeze of the intervention price, it seems odd to contemplate increases in the liquid milk premium. The "potential difficulty" which the Chancellor mentions in relation to distributors' margins is that if, under the Binder Hamlyn arrangements, these are increased, while the retail price is not, this will imply a reduced nominal wholesale price. If the retail price is not increased, it might be necessary (and fair as between distributor and supplier) to suspend the Binder Hamlyn arrangements.

We cannot be seen to be encouraging our own dairy farmers to produce more while we are still trying to reduce the Community's milk surplus. We recommend no immediate increase in the retail price of milk.

NICHOLAS OWEN
20 December 1983

4.59

cc NO

Treasury Chambers, Parliament Street, SWIP 3AG
01-233 3000

20 December 1983

The Rt. Hon. Michael Jopling MP
Minister of Agriculture, Fisheries and Food

Dear Michael

LIQUID MILK PRICES

Thank you for your letter of 6 December proposing a 1p. increase in the maximum retail price of milk from 4 March, and a 2-stage adjustment to the wholesale maximum price.

I must say I am sceptical about the present arrangements which determine liquid milk prices. It is directly contrary to the general liberalising thrust of our policies to exercise precise control over this sector of the economy. Now that the industry is going to have to adjust to the possibility of imports of UHT and sterilized milk, this is a good time to reconsider the present regulatory approach in England and Wales. (In Scotland the system has of course already changed substantially). I feel there is a strong case for ending the whole complex of formal and informal controls over the liquid milk sector and allowing market forces to operate, although we must of course bear in mind that given the existence of the Milk Marketing Board and the dominance of a few large diary companies, the scope for competition may be limited.

I therefore welcome your proposal to review matters thoroughly next summer and autumn. I also note that it is your intention to consult colleagues "when it is clearer what conclusions are likely to emerge". On this question, I must ask that Ministers collectively be given the opportunity to consider the issues before you embark on substantive discussions with the industry.

I feel it would be appropriate in your present announcement to signal the possibility that the whole system could be ended; and to avoid the implication in your present draft that the outcome of the review has necessarily to be agreed with both sides of the industry. Obviously, it would be better if all concerned agreed on the way forward, but if this is not possible, it must surely be for the Government to decide its own policy. I therefore suggest amending your draft to read "I shall be reviewing the position again thoroughly next summer and autumn, in consultation with the interests concerned and taking account particularly of the effect of imports, with a view to deciding on whether and if so in what form statutory controls over milk prices should apply from Spring 1985 onwards".

I am afraid that I cannot at present agree to any increase the retail milk price. Milk is in chronic over supply within the European Community; it would be consistent with our policy of reducing the burden of agricultural support on consumers and taxpayers alike not to increase the liquid milk premium. I recognise that there may be a potential difficulty with the question of the distributors' margins, but I do not think this should be an overriding consideration. I would, however, suggest that it is another good example of the need for a radical review of the whole system.

I am sending copies of this letter to the recipients of yours and to Geoffrey Howe and Norman Tebbit.

NIGEL LAWSON

EURO ~~POL: CAP~~

~~Pt 12~~

20 DEC

BF/ with Treasury response   cc ~~NO~~

NORTHERN IRELAND OFFICE
WHITEHALL
LONDON SW1A 2AZ

SECRETARY OF STATE
FOR
NORTHERN IRELAND

The Rt Hon Michael Jopling MP
Minister of Agriculture, Fisheries
and Food
Whitehall Place
LONDON
SW1A 2HH

19 December 1983

Dear Michael

LIQUID MILK PRICES

Thank you for copying to me your letter of 6 December to Nigel Lawson. I can see that you have had a difficult round of negotiations on this matter this year but I think that in the end you have come up with a package which represents a fair division between milk producers and the dairy trade while at the same time taking account of the interests of consumers.

Accordingly I agree to the issue of your statement along the lines suggested in your letter. I also agree to your proposal to review the current arrangements next year in the light of imports of milk. It will of course be important to take full account of the implications for the industry in Northern Ireland of any changes in the current system.

I am copying this letter to the Prime Minister, Nigel Lawson, George Younger, Nicholas Edwards and Sir Robert Armstrong.

Yours

Jim

~~Euro Pol: CAP~~

~~Pt 12~~

19 DEC 1983

cc DO

BF with Treasury reply AT 16/12

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

The Rt Hon Nigel Lawson
Chancellor of the Exchequer
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

6 December 1983

Dear Nigel.

LIQUID MILK PRICES

I have now completed the usual autumn review of liquid milk prices in the light of the latest costing results and other relevant data in consultation with the interests concerned. These discussions have been rather more protracted than usual because both sides of the industry face major uncertainties and problems.

The dairy trade are very concerned about the economic implications for them of the Government's decision to admit imports, made inevitable by the adverse Judgment of the European Court. They have also argued strongly that the revised Binder Hamlyn costing arrangements have operated more harshly than is reasonable or they had expected and have pressed for a major change in the averaging and sampling arrangements to redress the balance in their favour.

I have rejected this suggestion but I do recognise that there is considerable concern on both sides of the industry about the possible effect of imports and I have agreed that there should be further discussions next summer or in early autumn to assess the effect of imports and to consider what changes, if any, in our current arrangements it may be appropriate to introduce in order to deal with the new situation as it develops.

Milk producers, who last year had, partly because of favourable weather, a good year which, for the first time since 1977/78, broke the trend of steadily declining net margins, have now had a difficult

/year. The latest ...

year. The latest figures, which I enclose, show a resumption of the sharp declining trend of net incomes to levels in real terms very substantially below those in the latter two years of the last Labour Government. Moreover, these figures take no account of any further measures that may have to be imposed on milk producers as a result of current Brussels negotiations. This prospect has produced strong pressure from milk producers for some early boost to their returns.

Faced with these exceptional difficulties and uncertainties, and bearing in mind your concern to bring down the rate of inflation, I have concluded that the best course is to make a milk price determination over a somewhat longer period than usual and to make a retail price increase significantly below the usual trend. I intend to use the brief breathing space that this should give us to review our present arrangements more fundamentally taking account of the current pressures on the industry and its changing circumstances. Naturally I will consult my colleagues in due course when it is clearer what conclusions are likely to emerge from this work.

As regards the immediate price determination what I have in mind is to make an increase of 1p/pint in the retail price on 4 March 1984. This will be the first increase since November 1982 and this represents an annual increase of only 3.7% compared with your recently announced estimate of a year on year inflation rate of around 5.5% in the first half of next year. I would hope to be able to hold this price through to the first quarter of 1985.

On the basis of the latest costing results and capital survey projected forward to the end of March 1985 we expect the dairy trade to be undercouped at present prices by some £50 million. With the aim of ending up broadly all square at the end of this period I propose to increase the present maximum wholesale price (17.983) by 0.45 ppl on 1 January and again by 0.46 ppl at the beginning of March when the retail price goes up. The effect of these changes will be to give producers a little over half the proceeds of the retail price increase.

During the 18 months period from October 1983 to March 1985 we shall continue to operate the costings and capital surveys as previously. However, in order to preserve the price envelope I have set out above and to seek to give the industry a stable basis for planning in that period, I have agreed with the industry that if our present projections turn out to be not exactly in line with the actual results of the next round of costing and capital surveys any difference in either direction will be written off in relation to the period up to March 1985. The data collected in this period will however be carried forward into the following period as the basis of subsequent projections subject to any changes in the arrangements that may be agreed upon as a result of the discussions next summer and autumn.

I believe that the arrangements set out above strike a fair balance between the interests of milk producers, the dairy trade and consumers and take account of the importance of reducing the

/rate of inflation. ...

rate of inflation. If you and the other colleagues to whom I am copying this letter are content with them I would propose to make
... an early statement on the lines of the enclosed draft.

I am sending copies of this letter to the Prime Minister, George Younger, Jim Prior, Nicholas Edwards and Sir Robert Armstrong.

Yours Ever

Michael

MICHAEL JOPLING

NET MARGINS FOR MILK IN ENGLAND AND WALES

April/March year	1975/76	1976/77	1977/78	1978/79	1979/80	1980/81	1981/82	1982/83	1983/84 estimate*
£ per cow - money terms	103	67	121	116	98	111	122	167	109
- real terms	100	56	89	79	67	56	55	73	45
Yield per cow (litres)	4326	4396	4598	4819	4860	4948	4913	5196	5070

Assumptions

* Assumes no change in liquid milk prices. 6% increase in milk Producers' costs.

MILK AND MILK PRODUCTS DIVISION II
November 1983

DECEMBER 1983

LIQUID MILK PRICES

In a Written Reply to a question by [ ], in the House of Commons to-day, asking whether he had completed his autumn review of liquid milk prices, the Rt Hon Michael Jopling, MP, Minister of Agriculture, Fisheries and Food said:

What information? Surplus

"I have now completed the annual autumn review of milk prices in the light of the latest information on costs and conditions in the industry in consultation with representatives of milk producers and the dairy trade and with regard to the consumer on whom they both depend. but not in consultation with the consumer.

I have come to the following decisions:

(i) the maximum retail price will be increased by 1 penny a pint to 22 pence a pint on 4 March 1984: this will be the first increase since November 1982 and represents an annual increase of only 3.7%; — too high.

(ii) the maximum wholesale price will be increased with effect from the beginning of January by 0.45 pence a litre to give producers a little extra help them through the winter and by a further 0.46 pence a litre with effect from the beginning of March when the retail price change takes place.

(iii) the dairy trade's target rate of profit for the milk costings year 1983/84 which started on 1 October 1983 will be increased from 0.9048 pence per litre to 0.9860 pence per litre. This results from the comparison with the rate of return on comparable groups of food manufacturing and retailing companies provided for under the Binder Hamlyn system.

They can't produce a surplus. They have to sell to the customers.

It is my hope that it will not be necessary to make further changes to these maximum milk prices until the early part of 1985. I

/have

have taken a longer perspective than usual in making these price determinations because I want the industry to be able to face the period of adjustment following the admission of imports with confidence and certainty. I shall be reviewing the position again thoroughly next summer and autumn with the interests concerned taking account particularly of the effect of imports with a view to agreeing on the arrangements that should apply from spring 1985 onwards.

Statutory Instruments giving effect to these new maximum prices will be laid before Parliament in the normal way.

NOTES FOR EDITORS

1. Present maximum prices for liquid milk were announced on November 5, 1982 in Press Notice No 393.

2. The present maximum wholesale price is 17.983 ppl.

3. These decisions do not affect milk prices in Scotland which are subject to separate legislation.

NEW ST. ANDREWS HOUSE
ST. JAMES CENTRE
EDINBURGH EH1 3SX

2

Prime Minister

The Scots agree that this price increase will have no effect on retail milk prices.

MCS 28/3

John Gieve Esq
Private Secretary to the
Chief Secretary to the Treasury
HM Treasury
Parliament Street
LONDON
SW1P 3AG

25 March 1983

Dear John,

LIQUID MILK PRICES

I enclose the text of an announcement which my Secretary of State intends to make in the form of a Written Reply next week notifying an increase in the maximum statutory Boards' first-hand selling price of milk for liquid use in Scotland to 21 p/litre from 1 May 1983.

Robert Lowson's recent letter notified you that the Minister of Agriculture, Fisheries and Food would announce that no change in the retail or wholesale price of liquid milk in England and Wales was to be made. As you are aware from previous correspondence on this subject, the system of liquid milk pricing differs in Scotland and our announcement, of which MAFF are aware, will have no effect on milk prices in Scotland. The increase in the wholesale price, which in Scotland is a "true maximum" (and not an actual figure which the parties involved actually observe) is necessary to allow the Milk Boards and the buyers of milk sufficient freedom to negotiate an actual price. The current maximum is now too close to the expectations of the Milk Boards, as a recent arbitration claim by the Scottish Milk Marketing Board has shown and the scope for free negotiation could be curtailed if the maximum is not increased.

The Order sets a time limit to ensure that all parties involved in milk price negotiations are aware that we shall have to act on the Order by that date, whether arbitration procedures are then in progress or not. Previous experience has shown that if it became desirable to amend the Order while an arbitration was under way the parties involved could construe our action as an indication of the Government's view of the arbitration. This we wish to avoid; the time limit is intended to achieve this end.

I am copying this letter to Willie Rickett (No 10), Nick Huxtable (Lord President's Office), Robert Lowson (MAFF), John Lyon (Northern Ireland) and Adam Peat (Welsh Office).

Yours,

Muir

A MUIR RUSSELL
Private Secretary

ANNEX C

LIQUID MILK PRICES

Written Question

To ask the Secretary of State for Scotland, if he will now make a statement about the level of milk prices in Scotland.

Draft Reply

I propose shortly to lay an Order which will raise the maximum Boards' first-hand selling price from its current level of 19p/litre to 21p/litre. The ex-dairy price of 124p/gallon in Scotland will remain unchanged. The increase will have effect from 1 May.

As I indicated in my reply of 16 April, 1981[1] to my hon Friend the Member for Argyll, the Government have withdrawn control from the maximum retail, doorstep delivered price of milk in Scotland. Since then, we have set only a maximum ex-dairy price and a maximum level for the Boards' first-hand selling price for milk for liquid use. In my reply of 29 March 1982[2] to my hon Friend, the Member for Moray and Nairn, I indicated that the maximum Boards' first-hand selling price control should thenceforth be regarded as a true maximum within which the parties directly concerned in the operation of the market should negotiate an actual appropriate price in the light of commercial realities.

It is now clear that in order to enable the parties directly concerned sufficient freedom to negotiate actual prices in the light of commercial circumstances, an increase in the maximum Boards' first-hand selling price is required. I remain of the view that the actual prices in Scotland are a matter for the Joint Committees in the respective Milk Marketing Board areas.

I propose in the Order that the maximum prices will apply until 31 December 1983. This will indicate to all parties concerned that the Government will review the appropriate levels by that date to ensure that they remain true maximums.

[1] [illegible].P. 16.4.81 Vol 3, Col 228-9

[2] [illegible]

1

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's Private Office

CONFIDENTIAL

Private Secretary to the Chief
Secretary to the Treasury
Parliament Street
London
SW1P 3AG

1 Mr Scholar
2 Prime Minister

24 March 1983

I should think so! We have only just put it up and earlier than usual!

WR 24/3

Dear Private Secretary

LIQUID MILK PRICES

I enclose the text of an announcement that my Minister intends to make in the form of a Written Parliamentary Reply at mid-day on Friday, 25 March. As you will see he has decided that no change in either the retail or wholesale price of liquid milk is justified on this occasion.

I am sending copies to Willie Rickett (No 10), Nick Huxtable in Mr Biffen's Office, John Lyon (Northern Ireland Office) and Adam Peat (Welsh Office).

Yours ever

David Dawson

for R LOWSON
Principal Private Secretary

LIQUID MILK PRICES

Written Question

To ask the Minister of Agriculture, Fisheries and Food if he has completed his spring review of liquid milk prices.

Draft Reply

I have now reviewed the level of liquid milk prices in the light of the latest information available on costs and conditions in the dairy industry in consultation with representatives of milk producers and the dairy trade. I have decided to make no changes in the current maximum retail or wholesale prices on 1 April.

These prices will be further reviewed in the autumn in the usual way.

SUBJECT

CONFIDENTIAL

Agriculture

cc Mr Vereker
Mr Ingham.

cc Master

10 DOWNING STREET

From the Private Secretary

2 November 1982

Dear Robert,

Liquid Milk Prices: 1982 Autumn Review of Costings and Capital Employed

The Prime Minister held a meeting about liquid milk prices on 1 November. Your Minister, the Lord President of the Council and the Chief Secretary to the Treasury were also present.

After discussion it was agreed that the retail price of milk could go up by a maximum of 1p. per pint from 14 November. Your Minister would be telling the diary trade about this before then, probably on Thursday of this week. He would make an announcement by Written Answer on Friday 5 November.

I am sending copies of this letter to the Private Secretaries to the Secretaries of State for Northern Ireland, Scotland, Wales and to the Lord President and Chief Secretary, and Sir Robert Armstrong.

Yours sincerely,

Michael Scholar

Robert Lowson Esq
Ministry of Agriculture, Fisheries and Food.

CONFIDENTIAL

Please add the Lord President.
MT.

10 DOWNING STREET

(1)

Prime Minister

When we discussed milk on Thursday you said that a discussion with colleagues would be needed before you could agree to any increase in milk prices.

Mr Walker was very keen to have one on Monday for what seemed powerful reasons.

You will need the Chief Secretary. Anyone else (Mr Tebbit's RPI responsibility is primarily for the technicalities)?

MCS 29/10

Agriculture

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

CONFIDENTIAL

PRIME MINISTER

29 October 1982

Dear Prime Minister

it was at the specific request of Mr Walker's Office that I held back the earlier papers until his minute of 27/10 arrived, TLS

I am sorry that just before you went to Bonn you were confronted with the papers on milk for the first time.

I am in considerable difficulty over this. Last year we introduced revised Binder Hamlyn arrangements following tough negotiations with the Dairy Trade Federation in which the Treasury view, shared by ourselves, was imposed upon them. We can boast as a result of imposing Binder Hamlyn that a very substantial saving, probably something like £25 million, will be taken from the profit margins of the dairy trade.

Having set up the enquiry and announced our acceptance of its recommendations I am very anxious that on its first application I am not accused of incompetence.

Theoretically we should have announced our changes at the beginning of October but there was a delay that the dairy trade accepted as a result of the negotiations that were taking place. Understandably the trade are now very impatient having had our views imposed upon them and are insisting that the adjustments that we should have made on 1 October are now made.

The Dairy Trade Federation have a meeting next Wednesday and I am sure that it is essential that my decision is made before then. I am therefore very grateful to you for agreeing to meet me on Monday.

The amount to be paid to the Dairy Trade Federation is totally fixed by the Binder Hamlyn agreement imposed by the Treasury and ourselves

/upon the Dairy Trade ...

CONFIDENTIAL

upon the Dairy Trade Federation. If we give the Dairy Trade Federation the money due to them but put the retail price up by only 1p/pint in January, then the price paid to milk producers would have to be reduced. This would mean that the milk producer would be getting less for liquid milk in the period January - March 1983 than in the same period of 1982. This would be indifensible. Taking the index of milk producers' real incomes in 1977/78 as 100, they came down to 89 the following year; for each year since we have been in office they have been 65, 63, 62, and this year, with very good weather conditions, we currently anticipate that they will be 72. The proposals I originally put of a 1½p/pint increase in January reducing to a 1p/pint in June will mean, according to our estimates, that in 1983/84 they would be in the 66 - 72 range.

Leon Brittan thought that this was unacceptable because he would prefer to have a smaller increase earlier, and considered that the 12 month comparison was of no great importance, the important factor being the actual percentage increase. He preferred having a 5% increase sooner rather than 7½% later, reducing to 5%. I met Leon and I agreed to accept the Treasury view and go for a 5% increase from 7 November. The result of this would have been a slight deterioration in our income forecast, with our estimate for producer incomes in the coming year probably in the 64 - 70 range.

Due to the fact that I am now unable to announce our decision today it will not now be possible for any increase that we do agree to come into effect on 7 November. The earliest date would now be 14 November, leading to another small reduction in our projection of dairy producers' incomes.

We need either to use the Treasury solution and swiftly increase the retail price by 1p/pint, or the solution that I originally offered which will result in an actual reduction in the retail price next June and a very favourable record compared with the inflation rate by that time.

I am grateful to you for agreeing to a meeting at 6.30 pm on Monday and I am sorry that you should be troubled with such a matter.

✓ I am sending copies of this letter to Leon Brittan, Jim Prior, George Younger, Nicholas Edwards and John Biffen.

Yours sincerely

R. Lawson

for PETER WALKER
(Dictated by the Minister
and signed in his absence)

FILE CONFIDENTIAL

Agriculture

10 DOWNING STREET

From the Private Secretary 28 October 1982

Dear Robert,

Liquid Milk Prices: 1982 Autumn Review of Costings and Capital Employed

The Prime Minister was grateful for your Secretary of State's minutes of 18 and 27 October. She was also grateful for the Chief Secretary's minute on the same subject of 20 October.

The Prime Minister does not accept that there should be an increase in the retail price of milk on 7 November. She is opposed to an increase less than 12 months since the last increase, and would prefer the date of an increase to be postponed until after the schoolchildren return to school after the Christmas holiday. Mrs. Thatcher would like to have a discussion of this with your Minister and we are arranging this for Monday 1 November.

I am sending copies of this letter to John Gieve (HM Treasury), John Lyon (Northern Ireland Office), Muir Russell (Scottish Office), Adam Peat (Welsh Office) and Richard Hatfield (Cabinet Office).

Yours sincerely,

Michael Scholar

Robert Lowson, Esq.,
Ministry of Agriculture, Fisheries and Food.

CONFIDENTIAL

2 pp's.

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

CONFIDENTIAL

PRIME MINISTER

27 October 1982

Prime Minister

LIQUID MILK PRICES: 1982 AUTUMN REVIEW OF COSTINGS AND CAPITAL EMPLOYED

Further to my minute and the minute of Leon Brittan on the subject of the price of milk, Leon and I have agreed that the right course would be to make a 1p/pint increase of the maximum retail price on 7 November and we would increase the maximum wholesale price by 0.2p in order to restore the cut that was made last spring in this price.

This will meet the margin requirement which results from the new Binder Hamlyn system now agreed, and unless there are some unforeseen circumstances it should enable us to hold the retail price for a year.

I do have an urgent need to make this announcement in order that the trade can organise to meet the changes and I intend making this late on Friday afternoon.

I am sending copies of this minute to Leon Brittan, Jim Prior, George Younger, Nicholas Edwards and Sir Robert Armstrong.

pp PETER WALKER
(Dictated by the Minister and signed in his absence)

Agriculture : Wholesale Milk : Pt 2

CT 1982

Michael

With reference to your note below the answers are as follows:-

Scottish Office — no comments

Wales — hope to send a letter by this evening

Northern Ireland — will have comments but will not be available until 26th Oct '82

Are you content to wait for their comments?

Yes

Steve

22/10/82

CHIEF SECRETARY TO THE TREASURY

PRIME MINISTER

LIQUID MILK PRICES: 1982 AUTUMN REVIEW OF COSTINGS AND CAPITAL EMPLOYED

attached.

Peter Walker minuted you on 18 October concerning his proposals for raising liquid milk prices. It may be helpful if I set out my reaction.

2. I can confirm that the Treasury is content with the detailed method which has now been negotiated for the future determination of the target rate of profit of the dairy trade. I am particularly pleased that it has proved possible to proceed on the basis of full CCA data. You will recall that I had serious reservations about the adjusted HCA basis used last year.

3. The position of producers clearly is substantially improved this year. Following last year's below average position, yields have broadly returned to trend and incomes have been boosted by price increases (including the impact of last year's CAP price-fixing settlements on returns from manufactured products) rising faster than costs. I note that real returns remain somewhat below earlier peaks, but the fact remains that they are higher than in any of the three last years - a position that contrasts markedly with large parts of the private sector. No doubt producers would not welcome a reduction in their returns, but I do not think we can or should automatically rule out that possibility.

4. I recognise the efforts Peter has made in constructing retail price proposals which are not out of line with the encouraging downward trend of inflation or which would further discourage milk

consumption. Nonetheless, I am concerned that the two-stage proposals would not be consistent with the general inflation prospect. The year on year rate of increase for the RPI is now falling quite fast, and there seems a good chance that it will now be below 6% by the turn of the year. To announce a regulated milk price increase of 7½%, even linked to a partial reduction later in the year, would pose major difficulties; however carefully the presentation was treated, it is the immediate 7½% that would have the impact rather than the promise of things to come later in the year. We must also not overlook the risks of further depressing milk consumption, particularly given the possible implications for the doorstep delivery system, to which I know Peter attaches great importance.

5. I therefore think we must restrict the increase to 1p per pint, a rise of 5%. I recognise the points Peter makes about an increase of that size in January. But as far as possible under-recoupment for the dairies is concerned, I do not think we need regard the precise period to 31 March 1983 as totally immutable. Presumably it would be possible to postpone the final small element of the recoupment until April without undue difficulty. We should also bear in mind that, under the new target rate of profit formula now agreed, the precise amounts estimated to be due to the dairies for the period to March are provisional figures and subject to retrospective adjustment; given the faster than earlier expected deceleration in the rate of inflation the assumptions on which the projections are based may well now be pessimistic. As far as producer prices are concerned, I certainly see no great difficulty about a standstill and, as noted above, I would not rule out a modest reduction.

6. If, despite these considerations, you and the Agriculture Ministers still regard a 1p increase in January as unacceptable, I believe there is a further option which remains substantially preferable to Peter's proposals. Peter is anxious to complete 1982 without a further milk price increase. Naturally I sympathise with this aim and the reasons for it, particularly the desire to avoid an increase less than 12 months after the last. Nonetheless,

I think it would be better to have a 1p increase with effect from the beginning of December than a 1½p increase in January. These two options would generate virtually identical additional revenue during the period to 31 March, and so fully meet Peter's concern about recouping the dairy trade. But the former option could legitimately be presented as an increase over approximately 11 months equivalent to less than 6% at an annual rate and therefore in line with, rather than above, the prevailing general rate of inflation. Some observers clearly could unfavourably contrast the milk price in December 1982 (21p) with December 1981 (18½p) and point to a 13½% increase. But that effect would last only one month and, as I have indicated, I think this would be preferable to living with a 7½% increase on the same basis throughout the first half of 1983. And it would be possible to include in the announcement our intention not to adjust the retail price again for at least a further 12 months.

7. I am sending copies of this minute to Peter Walker, Jim Prior, George Younger, Nicholas Edwards and to Sir Robert Armstrong.

L.B.

LEON BRITTAN
20 OCTOBER 1982

Agriculture: Milk Prices Pt 2.

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

CONFIDENTIAL

PRIME MINISTER

18 October 1982

Prime Minister

LIQUID MILK PRICES: 1982 AUTUMN REVIEW OF COSTINGS AND CAPITAL EMPLOYED

You will remember that, following consideration of the third Binder Hamlyn report, we took decisions last December about the costings system on which our control of maximum prices for liquid milk rests. In particular, we decided that, in future determinations of the target rate of profit of the dairying trade should rest on comparisons with the rates of return in comparable groups of food manufacturing and retailing companies. Last year the determination had to be based on adjusted historic cost accounting (HCA) data because of the lack of current cost accounting (CCA) data in the dairying industry, but we decided that future determinations ought if possible to be put on a fully CCA basis, failing which we should have to rely on unadjusted HCA data. The aim of these changes and the other detailed recommendations of Binder Hamlyn which we accepted was to put the determination of the dairying trade's margin and target rate of profit on a more objective and predictable basis, while creating the greatest possible incentive to efficiency in these arrangements.

All parties concerned preferred to operate on a full CCA basis. Accordingly the dairying industry commissioned the necessary revaluations and Binder Hamlyn were instructed to undertake a new study of capital employed in the industry and to make the necessary comparisons with the reference industries. The results of these studies were then combined with the normal annual costings study and projection exercise on the basis of the Binder Hamlyn improvements agreed last year and certain other further changes (particularly affecting the treatment of depreciation) necessary to put the whole calculation on a fully CCA basis. As a result of this work we have established a new CCA based system which

/for 1982/83 ...

CONFIDENTIAL

for 1982/83 produces a target rate of profit of 0.9048p per litre. I believe that this method of calculation and the figure resulting from it will be acceptable to both sides of the industry and to the Treasury who have been closely consulted at official level by my people on this. Without going into the considerable complexities of the detailed calculations I should perhaps explain that this target rate of profit figure cannot be directly compared with last year's figures because of the change of basis of the determination. However, when the target rate of profit is taken together with depreciation, as it must be to get a fair basis of comparison the result is that the total cash flow to the dairying industry on these two items is increased by only 3.2% as a result of the stricter basis of determination now adopted.

When combined with the costings results and projections, and after allowance for depreciation charges, this would correspond to an underpayment to the dairying trade in the period up to 31 March 1983 (ie the mid-point of the milk year) of some £29 million if there were no change of milk prices in that period. The decision we now have to take is what adjustment of milk prices we should make to enable the dairying trade to recoup this shortfall and to provide a fair apportionment of return to milk producers, bearing in mind also the interests of consumers and the impact of milk price increases on the retail price index.

For the first time since we took office, milk producers have had a rather easier year, partly because of better weather, following 4 years of mounting indebtedness and steady and significant erosion
... of their real net margins. I enclose the relevant figures. However, the modest recovery of margins forecast for 1982/83 falls appreciably below the levels in the latter two years of the last Government and the prospect for increased returns from the manufacturing sector, on which they still depend for around half their income, is uncertain given that the next Community price-fixing will take place in the context of growing imbalance in the Community market for milk products indicating a clear need for price restraint.

As a result of the improvements we secured last year in the margins and costings system I was able, in my Spring determination of milk prices, to make a smaller cut (of 0.2 ppl) in the maximum wholesale price than hitherto. This helped to restore the confidence of milk producers in the operation of the margins and costings system. However, I think they would be very dismayed if as we approach the period of the year when their costs are highest we were to make a further cut in the wholesale price rather than giving them a small increase in returns.

/So far as ...

CONFIDENTIAL

So far as the consumer is concerned, I am anxious to complete 1982 without an increase in the price of milk. It is clearly important not to make an increase in the retail price which is out of line with the recent encouraging downward trend of inflation or which would give excessive discouragement to consumption of liquid milk. It is also desirable if possible to avoid timing an increase in such a way as to produce a high year on year percentage increase which would happen if we put the retail price up before the beginning of January.

Against this background I have considered various possibilities. A 1½p/pint increase on 9 January would be the ideal solution. This would generate some £36.5 million in the period up to 31 March 1983, enough to recoup fully the dairying trade's £28 ~~£29~~ million margin shortfall and to leave some ~~£7.5~~ million £8.5 to be distributed to the dairying producers. An increase of 1½p/pint would, however, represent an increase of 7½% over the present retail price compared with the Chancellor's latest end-year forecast of 6½%. However, a 1p increase on 9 January, a year on year increase of 5%, would yield only about £24.5 million leaving the trade ~~£4~~ 3.5 million unrecouped and the milk producers empty handed.

As a 1¼p/pint increase is not available to us for numismatic and other reasons, I have concluded that the best course is to make a 1½p/pint increase on 9 January and then reduce the price by ½p/pint on 5 June. This would give an average price over 1983 which would represent a 6% increase compared with the present price of 20p/pint and in June it would mean that the price of milk had increased by only 5% over 18 months. It would enable the dairying trade's margin requirement to be fully met in the period up to 31 March 1983 and enable a modest increase to be made from 9 January in the maximum wholesale price as well as generating a certain amount of income in the summer months which should help to defer the need for a further retail price increase for some time.

Although this would be a somewhat unusual pattern of price change I think it would meet the political and other requirements of the situation and if you and the other colleagues to whom I am copying this minute are content I will clear an appropriate statement with them for early issue.

I am sending copies of this minute to Leon Brittan, Jim Prior, George Younger, Nicholas Edwards and to Sir Robert Armstrong.

John Hobbs

PP PETER WALKER
(Approved by the Minister and signed in his absence)

CONFIDENTIAL

PRODUCER NET MARGINS

	1972/3	1975/6	1976/7	1977/8	1978/9	1979/80	1980/1	1981/2	1982/3*
Net £ Margin/Cow	70	89	67	121	116	98	111	122	153
Real terms 77/8 = 100	127	99	63	100	89	65	63	62	72

*forecast assuming no change of milk prices.

Agriculture, Milk Prices, Pt 2

Agriculture

(2)

Prime Minister

MES 30/3

Treasury Chambers, Parliament Street, SWIP 3AG

Robert Lowson Esq
Private Secretary to
Rt Hon Peter Walker MBE MP
Minister of Agriculture,
Fisheries and Food
Ministry of Agriculture,
Fisheries and Food
Whitehall Place
London SW1A 2HH

MS

29 March 1982

Dear Robert,

LIQUID MILK PRICES

Thank you for your letter of 25 March. The Chief Secretary has seen the statement your Minister made on Friday about the change in the maximum wholesale price for milk, which has the effect of reducing the return to the producer and increasing the return to the dairy trade.

The Chief Secretary has said that he would not want to object to this relatively minor adjustment in the wholesale price. He has, however, asked me to say that he would normally expect the Treasury to be consulted about changes in the wholesale price, even where no change in the retail price is involved. He understands that in the present case Treasury officials had indeed asked to be consulted in advance of any discussions with the Dairy Trade Federation. He assumes that in taking the present decision your Minister is satisfied that the reduction in the producers' price will not significantly increase the pressures in the autumn for a further increase in the retail price of milk; not make it more difficult for the Government to make the adjustment to the distributors' margin which would be necessary if the Dairy Trades Federation are unable to introduce the full Current Cost Accounting arrangements referred to in the Government's statement of 22 December last year.

The Chief Secretary has noted your Minister's intention to make a further announcement about milk prices before 1 October this year. He assumes that this does not mean that any further increase in the retail price of milk would necessarily apply from 1 October, particularly given the hope expressed in your Minister's letter of 2 December last to the Chancellor that it will be possible to avoid any further increase for at least the greater part of 1982. He points out that a further increase within 9 months of last January's 1.5p increase would be difficult to reconcile with the Government's objectives for bringing down the rate of inflation.

Finally, the Chief Secretary has asked me to say that he attaches particular importance to there being full consultation with the Treasury on the autumn costings data and on the Dairy Trade Federation's proposals to move to CCA well in advance of any proposals being discussed with either producers or distributors.

I am sending copies of this letter to the recipients of yours.

Yours sincerely

Terry Mathews

T F MATHEWS
Private Secretary

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's
Private Office

1 MAP
2 Prime Minister 2

cc Mr Ingham

WR 25/3

T F Matthews Esq
Private Secretary to the
Chief Secretary to the Treasury
Parliament Street
London
SW1P 3AG

25 March 1982

Dear Terry

LIQUID MILK PRICES

My Minister will be announcing a seasonal decrease in the wholesale price of liquid milk in the form of a written Parliamentary Reply at mid-day tomorrow. He will also be sending copies of his announcement this afternoon to the Milk Marketing Board, the National Farmers' Union and the Dairy Trade Federation. I enclose a copy of the announcement that he intends to make.

I am sending copies of this letter and it's enclosure to Nick Huxtable in Mr Pym's Office and to Willie Rickett at Number 10.

Yours sincerely

Robert Lowson

R LOWSON
Private Secretary

The Government has been considering the level of liquid milk prices that should apply during the coming months, having regard to all the relevant considerations including the data available from the costings system and the changes which I announced on 22 December 1981 following the Binder Hamlyn review. In the light of these considerations, and of the normal seasonal variations in cost factors, the Government has concluded that it would be right to reduce the maximum wholesale price by 0.2p per litre with effect from 1 April. The new prices, which in the case of Northern Ireland also reflect the consumer subsidy there, will be as follows:

	p/litre
England and Wales (except London)	17.783
London	16.016
Northern Ireland	21.400

These prices will of course be further reviewed in the autumn when full account will be taken of the definitive costings data and of the position of milk producers. It is my wish to provide both milk producers and the dairy trade under the new costings system with a firmer basis for planning their commercial operations and to announce decisions promptly each spring and autumn. In conformity with this objective it is my intention to seek to announce before 1 October the prices to apply in the winter months.

A Statutory Instrument giving effect to these new maximum wholesale prices will be laid before Parliament shortly.

The maximum retail price will remain unchanged.

- 2 -

The Government has been considering [illegible] rates that should apply after [illegible] all the relevant considerations [illegible] the [illegible] following the [illegible] of [illegible] Government [illegible] [illegible] per [illegible] which in the case of [illegible] the consumer subsidy [illegible]

[illegible]

England and Wales [illegible]

Scotland [illegible]

Northern Ireland [illegible]

25 MAR 1982

[illegible]

A Statutory Instrument giving effect to these new maximum [illegible] will be laid before Parliament [illegible]

The maximum retail prices will remain unchanged.

Agriculture SAW FILE

10 DOWNING STREET

From the Private Secretary

21 December, 1981

Liquid Milk Prices

I attach a note of the meeting which the Prime Minister held this morning to consider the amount by which the maximum retail price of milk should be increased in January, and the method of calculating target rates of profit for the dairy trade.

I am sending copies of this letter to Terry Matthews (Chief Secretary's Office, Treasury), John Rhodes (Department of Trade), Muir Russell(Scottish Office), John Craig (Welsh Office), Stephen Boys-Smith (Northern Ireland Office) and David Wright (Cabinet Office).

M. C. SCHOLAR

Miss Kate Timms,
Ministry of Agriculture, Fisheries and Food

CONFIDENTIAL

Mr. Scholar

c Mr. Wright

MR GREGSON

Pg 21/12

LIQUID MILK PRICES

I attach a note of this morning's meeting for Mr Scholar to circulate. Copies should go to those present and to the Secretaries of State for Wales and for Northern Ireland.

D J L MOORE
21 December 1981

Attachment:

CONFIDENTIAL

NOTE OF A MEETING HELD AT 10 DOWNING STREET ON
MONDAY 21 DECEMBER 1981 AT 10:30AM TO
DISCUSS LIQUID MILK PRICES.

PRESENT

The Prime Minister

Minister of Agriculture, Fisheries and Food.	Secretary of State for Trade.
Chief Secretary, Treasury.	Minister of State, Scottish Office.

Mr P L Gregson
Mr D J L Moore

******

The Meeting discussed a minute of 14 December and a letter of 16 December to the Prime Minister from the Minister of Agriculture, and a minute of 16 December from the Chief Secretary, Treasury about the amount by which the maximum retail price of milk should be increased in January and the method of calculating target rates of profit for the dairy trade in the light of the recommendations in Binder Hamlyn's report of November 1981.

The Minister of Agriculture said that, following the meeting of the Ministerial Committee on Economic Strategy on 10 December (E(81)38th Meeting), he had agreed with the Chief Secretary that there should be a full re-assessment of the target rate of profit annually rather than every three years. He had not, however, been able to reach agreement on the other outstanding issues. He remained firmly of the view that there should be an increase of 1½p in the price of liquid milk to give a maximum of 20p a pint from 10 January 1982 and that the costings and target system should be based on approximate calculations of Current Cost Accounting (CCA) depreciation, as discussed in Binder Hamlyn's report, until such time as the trade could produce their own proper CCA calculations. To attempt to impose a lower price increase in January, or a system which squeezed the dairy trade's margins still further, would risk the breakup of the present system of controls on milk prices and the loss of door-step deliveries. As it was, his proposals were tough and had been accepted by the trade only after long, protracted and difficult negotiations.

The Chief Secretary, Treasury said that CCA approximations on the lines proposed would give the trade an unwarranted bonus in 1981-82 and an unquantifiable though certain gain thereafter. When Binder Hamlyn's report of November 1981 was made public it could be used to expose the deficiencies of a system based on CCA approximations. He recommended a price increase of only 1p from January 1982 and that, until such time as the trade could produce their own CCA calculations, the system should be based on historic cost depreciation.

The Prime Minister, summing up a short discussion, said that the meeting agreed that the increase in the maximum price of liquid milk should be of 1½p a pint from 10 January 1982 and that the dairy trade should be told that for one year the calculations would be on an approximate CCA basis, as set out in Binder Hamlyn's report of November 1981, but that thereafter they would be either on the basis of proper CCA calculations made by the dairy trade themselves or, pending such calculations, on the basis of historic costs. The aim was to give the dairy trade an incentive to put their accounts as quickly as possible on a CCA basis.

The Meeting -

1. Took note with approval of the Prime Minister's summing up of their discussion.

2. Invited the Minister of Agriculture, Fisheries and Food to agree with the Chief Secretary, Treasury the terms of his announcement to the House of Commons of their decision.

P.0619

PRIME MINISTER

Liquid Milk Prices

BACKGROUND

The papers before your meeting at 10.30am on Monday 21 December are the Minister of Agriculture's minute of 14 December and his letter of 16 December, and the Chief Secretary, Treasury's minute of 16 December. The issues are the amount by which the maximum retail price of milk should be increased in January and the method of calculating target rates of profit for the dairy trade in the light of the recommendations in Binder Hamlyn's report of November, 1981.

2. The Minister of Agriculture wishes to announce, in a Written Answer before the Recess, the Government's decision on the January price increase and its response to the Binder Hamlyn report. Before doing so he has to talk further with representatives of the trade about some of the details.

3. The system is complicated but, as background to the discussion, the main features are:

i. The distributive costings system, which will be amended to take account of Binder Hamlyn's recommendations, is designed to establish average costs by reference to a wide sample of dairies which excludes persistent loss makers.

ii. A target rate of profit is established in terms of x pence per litre; this target takes account of the separate target rates for milk processing, for wholesale sales and for retailing which are each calculated by reference to selected groups of food manufacturing and food retailing companies.

iii. Increases in maximum retail prices are announced periodically by the Government; the distributors' share of the yield is determined by the average costs and the target rate of profit, and the rest goes to the milk producers.

AGREED POINTS

4. At the meeting of the Ministerial Committee on Economic Strategy on 10 December (E(81)38th Meeting), it was agreed that the increase in the price of liquid milk should take effect after the school holidays but in time to be taken into account in the Retail Price Index for January, as had the corresponding increase in 1981. To meet this requirement the increase has to be no later than 12 January and, since it is the practice to increase milk prices with effect from a Sunday, the Minister of Agriculture proposes that the increase should be on 10 January.

5. The Committee were unable to take a decision on the amount of the increase, or on whether the Binder Hamlyn recommendations should be implemented as proposed. The Minister of Agriculture was asked to discuss these questions further with the Chief Secretary with the aim of ensuring that increases in milk prices were as low as possible but not such as to risk the break-up of the present system of controls.

6. The only point on which the two Ministers were able to agree was that there should be a full re-assessment of the target rate of profit annually rather than every three years with indexation in the intermediate years.

POINTS AT ISSUE

7. In their November 1981 report, Binder Hamlyn caluclated their proposals for the target rate of profit on the alternative bases of historic cost and Current Cost Accounting (CCA) depreciation. While they commend CCA in principle, they warn of the practical difficulties of implementing it at this stage for the dairy trade; they do not make a recommendation as to which is the preferred course.

8. The Minister of Agriculture recommends that the system should incorporate CCA depreciation and that the increase in the maximum retail price from 10 January should be of 1½p giving a total of 20p for a pint of milk. Of this, 1.1p would go to the milk producers and 0.4p to the distributors.

9. The Chief Secretary recommends that, until such time as adequate CCA data are available for the dairy trade, the system should be based on historic depreciation and that the January increase should be no more than 1p with the yield going to the

producers and not to the distributors. (NB 1p on a pint of milk leads to an increase in the RPI of 0.1 percentage points.)

10. Whichever method of depreciation is chosen, the trade's distributive margin will be substantially reduced by comparison with the present system. As the table at Annex 1 of the Minister of Agriculture's minute of 14 December shows, the reduction in the margin will be 0.42p per litre if CCA is used and a further reduction of 0.12p per litre if historic costs are used. Binder Hamlyn discuss this in paragraphs 6-9 and 45-53 of their report. They explain that the difficulty is that the dairy trade are not yet ready to adopt CCA in their accounts; they could do so only by a large amount of additional work which they have not the resources to undertake. They therefore recommend that if CCA is to be used it will be necessary to make an approximation by calculating the historic cost depreciation charge of each dairy and then scaling it up by reference to the ratio between historic and CCA depreciation charges of those companies in the chosen reference groups which have published CCA accounts (paragraphs 51 and 52). They warn that "it must be acknowledged, however, that the incorporation in this way of an estimate of CCA depreciation would introduce an additional element of approximation into the costing system which may not be regarded as acceptable".

11. The Minister of Agriculture defends his proposal on two broad grounds:

i. The use of CCA is right in principle, and Binder Hamlyn have produced a method for calculating it for the dairy trade.

ii. Whatever the technicalities, his proposals represent a package deal which is the best that can be negotiated with the dairy trade without risking the break-up of the present system of controls and withdrawal from door-step delivery. (He summarises in paragraph 5 of his minute of 14 December why the trade regards the package as severe enough already.)

12. The Chief Secretary argues that, until such time as satisfactory CCA accounts can be produced by the dairy trade, the system should be based on historic cost depreciation. His main arguments are:

i. CCA approximations would give the trade "an unwarranted bonus" of £17 million in 1981-82 and an unquantifiable though certain gain thereafter (see paragraph 6 of the Chief Secretary's minute.)

ii. Once Binder Hamlyn's report is made public, it can be used to expose the deficiencies of a system based on CCA approximations.

iii. Although historic costs will reduce the distributive margin yet further - to the benefit of the consumer - the fact is that the present system has allowed for unjustifiably generous margins.

OPTIONS

13. The system, and the arguments, are complicated and technical and without a detailed examination it is difficult to advise, or for Ministers to decide, on which is the right course. With that in mind, I think that your meeting is faced with a choice between three broad approaches.

14. First, you could agree to accept the Minister of Agriculture's proposals for both the system and for an immediate price increase of $1\frac{1}{2}$p. This decision could be justified on the grounds that, while the system was open to criticism in some respects, it represented a defensible package deal overall. It would be tougher on the trade than the old system, and so the consumer would be better off. It could be defended by reference to the detailed recommendations from Binder Hamlyn. The disadvantage of this course is that while it represents a better system than the present one, it could still be argued, on the evidence of Binder Hamlyn's own report, that it is a technically suspect system which is over-protective to the trade at the expense of the consumer. This is the point which the Chief Secretary makes.

15. Secondly, you could accept the Chief Secretary's recommendation of a 1p increase now - which he regards as a concession to the transitional difficulties of moving from the old to the new system - and a system incorporating historic cost depreciation until such time as CCA accounts are available in the industry. This could be represented as a yet better deal for the consumer and defended by reference to Binder Hamlyn's report. On the other hand, the Minister of Agriculture will argue that it is a high risk course which could lead to the break-up of the present system of controls and the end of door-step delivery. The discussion at E Committee on 10 December suggests that there is considerable support for this view.

16. The third possibility is to decide now what should be the price increase in January but to defer, pending further advice, a decision on the basis for the new system in the longer term. This would recognise both the importance of settling on a new system which Ministers were fully satisfied they could defend and also the difficulty of taking an immediate decision on the basis of the complicated and conflicting advice in the papers now before you. Logically a decision on the price increase should be deferred until any such further work had been completed. But Agriculture Ministers would undoubtedly bitterly resist this partly because of their concern over the effect on farmers' income of delays in the price increase. So the immediate increase might be allowed to go ahead on the understanding that it was without prejudice to the shape of the new long term system.

17. On this approach you would decide on Monday whether the increase on 10 January should be 1p or $1\frac{1}{2}$p. You would have to do so as a matter of broad judgement on what was the best balance between the needs of the trade and the producers on the one hand and of consumers on the other. The Minister of Agriculture could then announce this decision before Christmas and indicate that he would make a further statement on the implementation of Binder Hamlyn proposals as soon as possible in the New Year.

18. You could then ask the Minister of Agriculture and the Chief Secretary to arrange for further discussion by their officials and Binder Hamlyn of the arguments put forward on either side. The aim would be to establish, among other things:

i. whether CAA approximations as discussed in the Binder Hamlyn report could be publicly defended.

ii. whether it is possible to form a judgement on what difference in practice there might be between CCA calculations on the proposed approximate basis and proper CCA calculations made by the dairy trade themselves;

iii. whether, as a compromise, the dairy trade might be told that for, say, one year the calculations could be on an approximate CCA basis but that thereafter they would be either on the basis of proper CCA calculations made by the dairy trade or, pending such calculations, on the basis of historic costs; - the aim here would be to give the trade an incentive to put their accounts as quickly as possible on a CCA basis.

It would not be practical to complete such work in time to inform a decision on a price increase on 10 January, but I should think it ought to be possible to do so in time for decisions on the new system to be announced by, say, February.

19. If the meeting does agree that further work on these lines should be commissioned, you might like to consider whether you want some independent assessment of the further conclusions reached by Treasury and Ministry of Agriculture officials. One possibility would be to invite Mr K J Sharp, the Head of the Government Accountancy Service, to participate either as a member of the group or, perhaps, in the lead. Whatever his formal role in the group, I suggest that his advice should be made available to Ministers.

HANDLING

20. After the Minister of Agriculture has made his case and the Chief Secretary has replied you will wish to hear the views of the other Agriculture Ministers and also the Secretary of State for Trade who is concerned with the implications for consumers and for competition policy.

21. You might then consider the three broad options summarised in paragraphs 14-19 above.

CONCLUSIONS

22. You will wish to reach conclusions on which of the three courses should be followed. If you do decide on the third course - announcement before the Recess of a 10 January price increase and further work on the system - you will wish to ask the Minister of Agriculture:

i. to clear the text of his Answer with the Chief Secretary and the other Agriculture Ministers;

ii. to agree with the Chief Secretary on the details of how the further work should be carried forward and, if the meeting so wishes, to arrange for Mr K J Sharp to be involved.

23. The paper before E on 10 December, E(81)128, also recommended that the present premiums on Channel Islands and sterilised milk should be increased by $\frac{1}{2}$p per pint at the same time. E did not discuss this and the point has not been picked up in the present papers. I suggest that the Minister of Agriculture and the Chief Secretary can be left to settle this detail.

PG

P L GREGSON

18 December 1981

CONFIDENTIAL

Prime Minister

BINDER HAMLYN AND LIQUID MILK PRICES

As I will be unable to attend the meeting arranged for Monday I thought I should write to state my position on the points at issue. I have seen Peter Walker's paper of 14 December and Leon Brittan's paper of 16 December. I have also seen Peter Walker's letter of the same date.

I do not find Leon Brittan's technical arguments convincing and would most certainly disagree with his views on the impact on the dairy industry.

I think we should not under-estimate Peter Walker's success in his negotiations with the dairy trade. He has persuaded them to accept both a new system which will substantially reduce their level of remuneration this year and in years to come and also to forego £40m which would have been due under the old system for past years. As you will know I have some experience of this particular negotiation and I believe Peter has achieved a remarkable improvement.

I agree with his judgement that to turn the screw still tighter on the dairy trade would be very risky. If we try to do so the odds are that the trade will no longer co-operate in the system. This would inevitably mean that the trade would start to abandon the doorstep delivery system. I think it would be a grave mistake for us to get into a position where we could be blamed for the ending of this highly regarded institution.

I am copying this minute to our colleagues on 'E' Committee, and to George Younger, Nicholas Edwards and Sir Robert Armstrong.

pp J P

18 December 1981

(Signed on behalf of the Secretary of State in his absence)

CONFIDENTIAL

lf

010

Prime Minister

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

HLS 16/12

From the Minister

CONFIDENTIAL

PRIME MINISTER

16 December 1981

BINDER HAMLYN AND LIQUID MILK PRICES

The Chief Secretary has sent me a copy of his minute to you of 16 December and the paper he enclosed.

2. As our two papers will have shown, this is an extremely complicated subject. I would however like to emphasise just three points. First, the Chief Secretary's paper may give the impression that the proposed method of calculating the dairy trade's costs assures the trade that the total of these costs will be covered, together with a target rate of profit, however defined. This is not so. The costs will be calculated from a representative sample of dairies, whose results will be averaged arithmetically without any weighting for turnover or throughput. As it happens the larger units tend to have higher costs than the smaller largely because the larger ones tend to maintain delivery rounds in the big cities which are only marginally profitable. As a result, the arithmetical average understates true total costs, and deprives the trade as a whole of some £50m a year which they would get if the costs of particular enterprises went into the sample on a weighted basis. If the method of calculating profit is indeed somewhat more favourable to the dairies on the current cost accounting basis, this only partly makes up for the squeeze on their returns which results from the way in which costs for the trade as a whole are calculated.

3. Secondly, it is essential to see the problem in its proper context. If the system operated by the Labour Government and guaranteed to the trade by my predecessor had been maintained, the trade would have a legitimate claim to £40m, in respect of the period between my suspension of the system and 1 October 1980, which my proposals write off and withhold from them. Over the 18 months from October 1980 to next March my proposals give them £30m less than the Labour Government's system. And from next April they will get some £20m a year less than under the previous system. These figures show just how tough the proposals are. Little wonder that they have been so very hard to sell to the dairy trade.

/4. This brings ...

4. This brings me to the third and final point. There is in my judgement no way in which the dairy trade can be brought to accept any further squeeze on top of the very severe one I am proposing to apply. If we try to squeeze them further they will no longer consent to be bound by the price system. We cannot compel them to go along with it, and the result could in that case be chaos, leading to the eventual breakdown of the system of doorstep milk delivery. It would be politically very dangerous to the Government if that could be laid at our door. I am sure we should not take the risk.

5. I hope therefore that you and our colleagues will agree that we should go ahead with the tough proposals I have put forward.

6. I am sending copies of this letter to colleagues on E Committee and to Sir Robert Armstrong. I am also copying it to George Younger and Nickolas Edwards.

Yours ever

PETER WALKER

6 DEC 1981

(1)

Prime Minister

We now have both sides of the story. Should we

a) arrange a small meeting (Messrs Walker, Brittan, Younger, Edwards, Prior and Biffen)?

b) try to fit it into E on 22 December

c) or do you wish to make your mind up without a meeting?

I suggest a). Do you agree?

MCS 16/12

Yes

+ P Gregson
+ Moore
cos OH

PRIME MINISTER

BINDER HAMLYN AND LIQUID MILK PRICES

I have now seen the Minister of Agriculture's note to you on this subject. I am likewise attaching to this minute a short paper explaining my position on the CCA question and on the immediate increase in the milk price.

... 2. I am sending copies of both this minute and the attached paper to colleagues on E Committee and to Sir Robert Armstrong.

L. B.

LEON BRITTAN
16 December 1981

LIQUID MILK PRICES AND BINDER HAMLYN

Note by the Chief Secretary

Introduction

As recorded in the Minister of Agriculture's note of 14 December, he and I have been able to resolve one of the questions left unresolved by E Committee, namely whether the dairy trade's projected rate of profit should be indexed. On this we have agreed that there should be a full reassessment of the target rate of profit annually. I realise that this will incur a small additional cost; but it will enable us to assure the consumer that the new system is a fair one and that the dairies are not getting a level of protection against inflation greater than that available to other sectors of the economy.

2. There are thus two main issues left to resolve. First, whether the dairy trades' target rate of profit should be expressed in CCA or historic cost terms. Second, arising from that, what the immediate increase in the price of milk should be. In summing up at E Committee, we were asked to discuss these questions:

> "With the aim of ensuring that increases in milk prices were as low as possible, but not such as to risk the break-up of the present system of controls."

Historic v. Current Cost Accounting

3. The Minister of Agriculture's note accepts that the CCA calculation would give the dairies a total margin 0.12p per litre higher than the historic costs method. In terms of the immediate proposals, CCA would require an increase in the dairy trade's existing margin of 0.4p per pint whereas historic

costs requires a reduction of 0.3p per pint. In terms of cash, CCA is worth an extra £17m to the dairy trade in 1981-82 and an unquantifiable though certain gain thereafter.

4. This result is clearly anomalous. CCA is after all no more than a different way of presenting a business's financial position. As the Minister of Agriculture says, it is a method of accounting which presents a more reliable measurement of capital consumption and thus <u>in principle</u> gives a more realistic picture in a period of inflation. But CCA does not and cannot in itself alter the cash flow (ie profits <u>plus</u> depreciation) of a business to which it is applied.

5. This point is indeed brought out by Binder Hamlyn's calculation of the CCA adjustment for the two reference groups of food manufacturers and retailers. The table in Annex 1 below shows that, while the depreciation charge has risen and profits have been reduced, the overall cash flow (profits <u>plus</u> depreciation) for the reference groups remains unchanged. But there is no suggestion in Binder Hamlyn that the cash flow of the reference groups was inadequate in the period covered to maintain its fixed capital intact or that an <u>equivalent</u> cash flow would be inadequate for the dairy trade. In short, since Binder Hamlyn are clearly satisfied that the historic costs figures will give the dairy trades a satisfactory rate of return in comparison with the reference groups, there can be no justification for giving the dairies an extra £17m as a bonus merely through the application of CCA.

6. The reason why the Binder Hamlyn figures produce this £17m bonus lies in the method of calculation. They have calculated the ratios between historic and CCA depreciation and profits for the reference groups and have mechanically applied these ratios to the dairy industry, despite the fact that the latter's asset structure and rate of depreciation are substantially different from those of the reference groups. But the reference groups' CCA adjusted rate of profit stems from their much lower rate of

depreciation (23% of profits before depreciation as opposed to 35%). If the higher rate of depreciation on the dairy trade were allowed for, the historic cost and CCA cash flow figures would match. This is illustrated in Annex 2 below. It would indeed have been an extraordinary coincidence if Binder Hamlyn's method had produced the right result, ie. a reduction in profits balancing the increase in depreciation. Paragraph 4 of the Minister of Agriculture's note suggests that an anomaly of this kind would arise in any case, even if an actual CCA figure for the dairies' depreciation were available. But this would not be the case, so long as the higher rate of depreciation in the dairy trade is allowed for, as explained in Annex 2. It is no doubt considerations of this sort which led Binder Hamlyn to remark that the estimate of CCA depreciation made in their report:

> "Would introduce an additional element of approximation into the costing system which may not be regarded as acceptable".

7. It follows from what I have said above that I cannot agree to the CCA method being used to express the target rate of profit until such time as the dairy trade itself is able to produce its own CCA accounts. As I have argued above, to accept Binder Hamlyn's CCA method now would give the dairy trades an unwarranted bonus of £17m. To do this could well expose us to powerful criticism; once the Binder Hamlyn report is made available, there will be sufficient expertise in Parliament and the Press to ensure that the anomaly will be rapidly detected. In these circumstances Binder Hamlyn's defence - that their method of approximation is the best available - would be a lame one. The only defensible and objective definition of profits available to us must be the historic cost one. I should add that in taking this view I also have in mind the similar position we have taken in refusing to express the target rate of profit for non-competitive Government contracts in CCA terms, as long as the companies concerned cannot produce CCA accounts.

Impact of the settlement on the dairy industry

8. The Minister of Agriculture's note also argues, however, that irrespective of the view taken on the CCA, any attempt to squeeze the dairy trade's margin by the 0.12p per litre indicated on the historic costs method would not be acceptable to them and could lead to the break up of the present system of price controls. I accept that this is a difficult question of judgement. It is true, as the Minister of Agriculture points out, that implementation of Binder Hamlyn even on a CCA basis will mean that the dairy trade's profits will be lower by £40m than would have been the case under the previous system. But one of the reasons for suspending the old system was precisely the suspicion that it produced an excessive rate of profit. It is therefore difficult to see in what sense the £40m can be regarded as "owing" to the dairy trade. I recognise that the overall conclusions of Binder Hamlyn will certainly have been a disappointment to the dairy trades. But in at least two respects the Minister's proposals go some way to temper the outcome:

(i) the target rates of return for the dairy trades are not to be reduced because of the lower risk level, despite Binder Hamlyn's recommendation;

(ii) the costings figures are based on the average dairy's performance (excluding loss-makers) and not, as Binder Hamlyn recommended, on the more efficient dairies.

Taking these points into account, I believe that a settlement based on the historic cost approach could be presented to the dairies as a reasonable one.

9. The question we have to ask ourselves is whether the Dairy Trades Federation would readily abandon a system which guarantees them against the impact of any rise in their unit costs and in

addition, as I pointed out at E Committee, provides (even on a historic costs basis) what would seem to be very attractive rates of return on capital. My own guess is that they would be reluctant to cut themselves off from this system. Nor is it at all clear to me that a disagreement over the present price determination would have any immediate implication for the price control system or the doorstep delivery. As I understand it, the most likely reaction of the dairy trades would be to negotiate with the Milk Marketing Boards for a somewhat lower purchase price of their liquid milk. This would indeed be awkward, but would not seem to require the abandonment of price controls in the long term. Nor do I believe there would be a risk to the doorstep delivery system in the foreseeable future given the amounts of capital the dairy trades have tied up in it.

10. Nonetheless, I recognise that it would be over harsh to go for the immediate application of the full 0.3p reduction in the dairy trade's margin which is required by the historic costs approach. I would therefore agree to a phasing in of the new arrangements. My proposal is that the immediate price increase should be limited to 1p for the producers and that the dairy trade's margin should remain unchanged. Some further phasing of the adjustment process could certainly be considered at the time of the next review. Contrary to the suggestion in paragraph 7 of the Minister's note, I do not believe it would be all that difficult to give a convincing explanation of this approach. We would make it clear in any public announcement that we had based ourselves on the historic cost figures in Binder Hamlyn and, if necessary, give the reason why. We could then point to the excessive severity of an immediate reduction in the dairy trade's margin and explain that a phasing-in period was accordingly appropriate. In the meantime a 1p increase should provide adequate protection for the producers and be a helpful contribution to our objective of reducing the rate of inflation. It would no doubt also be particularly well received, given the recent Press speculation about an increase of 1½p.

L.B.

HM TREASURY
16 December 1981

ANNEX I

BINDER HAMLYN'S ADJUSTMENT OF REFERENCE GROUPS' ACCOUNTS FROM HISTORIC COSTS TO CCA

		FOOD MANUFACTURING		FOOD RETAILING	
		£m	%	£m	%
(a)	Profit before depreciation	1025	100	223	100
(b)	Historic costs (HC) depreciation	238	23	51	23
(c)	Profit after HC depreciation	787	77	77	77
(d)	Additional CCA depreciation	167	16	25	11
(e)	CCA profit	620	61	147	66

(f) = (b) + (d) + (e) = 1025 223, ie. = profits before depreciation

ANNEX II

Table (a) below sets out the historic costs and CCA depreciation and profits for both the reference groups and for the dairy trades on the correct assumption that the cash flow position of the two sectors is unchanged before and after CCA adjustment.

TABLE (a)

	Food Manufacturers		Food Retailers		Dairy Trades	
	£m	%	£m	%	profits	%
a) Profit before depreciation	1025	100	223	100	1.24	100
b) HC depreciation	238	23%	51	23%	0.43	35%
c) Profit after HC depreciation	787	77%	172	77%	0.81p	65%
d) Additional CC depreciation	167	16%	25	11%	0.27	22%
e) CCA profit	620m	61%	147m	66%	0.54p	43%

However Binder Hamlyn have calculated the CC target rate of profit for the dairy trades assuming an identical fixed asset structure and related depreciation charge of 23% of profits instead of the 35% shown in line (b).

This increases the CCA rate of return as follows:-	0.12	10%
	0.66p	53%

Binder Hamlyn's report, however, puts forward 0.81p per litre as a satisfactory profit target for the dairy trades in historic cost terms in comparison with the reference groups. If this is accepted, there can be no justification for increasing the CCA rate of return by the additionsl 0.12p, since this would imply a historic cost profit correspondingly higher than 0.81p.

16 DEC 1981

CONFIDENTIAL

P.1.

MR WRIGHT

Reference E 0294

cc Mr Gregson
   Mr Wentworth

1. Sir Robert Armstrong
2. Mr. Scholar No 10.

LIQUID MILK PRICES

At their meeting on 10 December E Committee agreed that the increase in the price of liquid milk should be after the school holidays but in time to be taken into the RPI for January. The Committee invited the Minister of Agriculture and the Chief Secretary to discuss further the amount of the increase and the new arrangements, in the light of Binder Hamlyn's recommendations, with a view to reaching agreement.

2. The Minister of Agriculture now reports, in the note attached to his minute of 14 December to the Prime Minister, that he has failed to reach agreement with the Chief Secretary. The Chief Secretary will now circulate - probably tomorrow morning - a note setting out his position. Since the Minister of Agriculture wants to announce to the House before Christmas the Government's decision on the immediate price increase and on the new system it will be necessary to have a meeting to break the deadlock.

3. At the meeting on 10 December the Prime Minister said that if necessary the matter would have to be resolved by a small group of Ministers. I suggest that such a meeting should now be convened under the Prime Minister, later this week if possible. In addition to the Minister of Agriculture and the Chief Secretary, the Secretaries of State for Trade, Scotland, Wales and Northern Ireland should be given an opportunity to come or to be represented. The alternative to such a meeting would be to put the matter back to E for discussion on Tuesday 22 December; in view of the complexity of the questions I would not recommend that. We will offer a brief when we have seen the Chief Secretary's paper.

DJLM.

D J L MOORE

15 December 1981

I agree.

RA 15.xii

CONFIDENTIAL

CONFIDENTIAL

Agriculture

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

Prime Minister

We await the Chief Secretary's side of this story.

MS 14/12

14 December 1981

PRIME MINISTER

BINDER HAMLYN AND LIQUID MILK PRICES

As agreed in E Committee on 10 December, I have had discussions with the Chief Secretary to the Treasury on the implementation of Binder Hamlyn and liquid milk prices. I attach to this minute a short paper setting out my position in the light of this discussion.

I am copying this minute and paper to our colleagues on E Committee.

Kate Timms

for PETER WALKER

CONFIDENTIAL

LIQUID MILK PRICES AND BINDER HAMLYN

Note by the Minister of Agriculture, Fisheries and Food

Introduction

1. Following our discussion in E Committee on 10 December, the Chief Secretary and I met this morning to consider the two aspects of my proposals on Binder Hamlyn which he considers to be unsatisfactory. These were :-

(a) that the dairy trade's target rate of profit should be indexed according to changes in the milk price during the 3-year intervals I propose between the full review of the capital they employ;

(b) that, until we have actual CCA data for the dairies, their CCA depreciation should be calculated (as Binder Hamlyn have suggested) by scaling up the historic cost charge.

Indexation

2. There are two aspects to this. In short term - ie for the period from 1 October 1980 up to and including the present 1981/82 costings year - we need some form of up-rating since Binder Hamlyn's measurement of the capital employed by the dairies relates to the 1980 calendar year, and is hence out of date. As regards the longer term, I still believe that a three-yearly review is preferable on the grounds that it is less burdensome for the industry and saves public expenditure in terms of accountants' fees. However, given the Chief Secretary's opposition to any suggestion of indexation, I am prepared to agree to an annual measurement of the industry's capital - though I should point out that this will cost us an additional £80,000 in each of the two intermediate years.

Historic v current cost accounting

3. Although the Treasury are in principle in favour of current cost accounting, they argue that the method used by Binder Hamlyn to arrive at CCA data for the dairy industry is unsound, and produces an anomalous result in that the reduction in the trade's margin arising from this

approach is some 0.12p per litre less than that using HCA depreciation (see Annex I) after the target rate of profit has been adjusted accordingly.

4. In purely technical terms, I would agree that it would have been better if we had had actual CCA data for the dairies. However, Binder Hamlyn have said that the use of CCA is a sensible step in principle in that it provides the more reliable measure of capital consumption, and they are perfectly prepared to defend the methodology by which they have arrived at their CCA depreciation figure of 0.70p per litre in line 2 of Annex I. It also has to be said that, even if we had an actual CCA figure for the dairies' depreciation, it does not necessarily follow that the overall balance between HCA and CCA would have been neutral. This is because the depreciation figures are based upon data from within the dairy industry, whereas the target rate of profit figures are derived from the experience in two other reference groups of food manufacturers and retailers, whose asset structures are similar to, but not identical with, the dairy trade. There is thus no guarantee that the difference between the two depreciation figures will precisely offset that between the two corresponding target rate figures.

5. I do not therefore accept the Chief Secretary's view that we should reject the CCA approach advanced by Binder Hamlyn. But, in any case, that argument has to be considered against the wider political background we face here. As my paper to E Committee indicated, we are already proposing - after long and protracted discussions with them - to squeeze the dairy industry very hard on Binder Hamlyn. Thus, in addition to writing off £40 million owing to them for the period up to 1 October 1980, I have -

(i) incorporated their wholesale results into the costings;

(ii) re-cast the costings sample, by cutting out persistent loss-makers and giving greater weight to the more profitable smaller dairies;

(iii) resisted strong pressure from the Dairy Trade Federation for a system based on weighted averages, which they claim - with some justice - would be a more realistic pointer to their overall position then one based on simple averages;

(iv) proposed a cut (in money terms) in their present target rate of profit, which (taken with depreciation) would reduce the distributive margin by 0.42p per litre, even using the approach opposed by the Chief Secretary.

6. Against this background, I am convinced that to reduce their margin by a further 0.12p per litre would not be acceptable to them, and that we would in that event face a break-up of the present system of price controls. Alternatively, if the Chief Secretary remains adamant that he cannot agree to the CCA approach recommended by Binder Hamlyn, we would need to find some other way to make good the 0.12p per litre deficit this would produce. In practice, this would mean either taking different groups so as to produce a higher target rate of profit, or setting the dairy trade's return by reference to a weighted average. The first of these would give rise to endless discussion about the composition of the reference groups, whilst the second would expose us on a point of principle of wide application within the costings, which would pave the way towards a much greater margin for the trade than any alleged gains they may receive from using CCA depreciation.

7. I am convinced, therefore, that, until such time as full CCA data is available for the dairies, we should implement Binder Hamlyn in the way I propose: indeed, I believe we have no practical alternative but to do so. In particular, the Chief Secretary and I did consider whether it might be possible for us to reach some agreement as regards the retail price and the amount going to the distributors in the immediate period to 1 April 1982, whilst making it clear that for any subsequent calculations pending full CCA costing we were intending to apply HCA figures. I am, however, opposed to this, partly because it would be extremely difficult to give a convincing explanation of such an approach, but also because it would mean that we should still find ourselves very shortly having to decide whether to apply to the dairy trade the sort of additional squeeze which in my view would break the system.

8. Against this background, and bearing in mind that we are dealing with an area which does not have any public expenditure implications, I hope the Chief Secretary will feel able to accept my judgement that

the proposals outlined in my paper to E Committee represent the very minimum the dairy trade can be expected to agree to if we are to maintain a viable costings system, and that we should proceed with a 1½p per pint increase in the retail price, subject to the timing point in the Prime Minister's summing up on 10 December.

HISTORIC v CURRENT COST ACCOUNTING

	HCA	CCA	Difference
			(p per litre)
1. Target Rate of Profit	0.81	0.66	- 0.15
2. Depreciation	0.43	0.70[(1)]	+ 0.27
3. Total (1+2)	1.24	1.36	+ 0.12
4. Present system	1.78	1.78	
5. Reduction (4-3)	0.54	0.42	- 0.12

<u>Footnote</u>

(1) In the absence of <u>actual</u> CCA data for the dairies, this figure has been derived by taking their HCA depreciation charges and up-rating these by a factor based upon the relative CCA and HCA depreciation charges for the two reference groups (food manufacturers and retailers).

10 DOWNING STREET

Prime Minister

The Treasury wanted this discussed at E next week not tomorrow, because they dispute MAFF's figures and believe the price increase could be smaller.

I pressed Mr Walker's office to agree to postponement but he was adamant that it needs to be ~~discussed~~ decided tomorrow, for political reasons (you were busy with Mobutu etc at the time). So I'm afraid the discussion may be difficult.

MCS 9/12

Confidential

Prime Minister

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

You asked for these figures at the weekend. (NB not copied to colleagues) MCS 9/12

From the Minister

9 December 1981

PRIME MINISTER

LIQUID MILK

You have asked for a table showing all the increases in the retail price of milk since May 1979, giving dates of the price increases, the total cash increase in each instance and the cumulative percentage increase.

These are set out in Table I attached, together with changes in the RPI and average earnings over the same period. They show an increase in milk prices slightly higher than the increase in the RPI. These figures are misleading, however, for two reasons. First, the milk price goes up in discrete steps, whereas the RPI and the earnings index go up gradually, since each reflects a multitude of individual price increases. To make a comparison fairly, it is therefore necessary to measure changes from and to the date of a milk price increase: the table you asked for takes as its base the price immediately before a large price increase, and its terminal date that immediately after the price increase proposed for January. This unfairly biases the comparison against milk. Secondly, the comparison is particularly deceptive because the price increase in June 1979 should under the Labour Government's own system have taken place on 1 April 1979. It was postponed by them for obvious electoral reasons.

If, in order to put the comparison on a fair basis, one takes as the base the date (November 1978) on which the price went up to the level at which we inherited it (13½p), then one gets the results in Table IA. As you will see, the increase in the milk price following my proposal would be less than the increase in the RPI over the same period and substantially less than the increase in average earnings (the figure for which would of course be higher if it were to be updated from its actual base of September 1981 to January 1982). I include figuresfor average earnings because of the labour-intensive nature of milk distribution. It is remarkable, in the light of this, that the January milk price is not a good deal higher. The reason it is not so is basically because I suspended the Labour Government's system and have declined to give the distributors the money that system would have given them; and because the new system I am proposing is far tougher on them.

You also asked for a table of monthly RPI increases in 1981 and in prospect. These are set out in Table II. I am afraid that the Department of Employment has not been able to give us monthly but only a quarterly figure for January-March 1982. The monthly figures for 1981 suggest however that January is the best month for the increase. It is most certainly needed on 3 January, for all the reasons set out in my paper for E Committee.

Yours
Peter

PETER WALKER

TABLE I

		MILK PRICE CHANGES					RPI	AVERAGE EARNINGS
DATE		(a)	(b)	(c)	(d)	(e)		
May	1979	-	13½p	-	-	100	100	100
3 June	1979	1½p	15p	£120m	11.1	111.1	101.7	102.7
17 February	1980	1½p	16½p	£ 77m	10.0	122.2	115.2	113.9
10 August	1980	½p	17p	£ 23m	3.0	125.9	124.4	127.0
4 January	1981	1½p	18½p	£165m	8.8	137.0	128.4	131.6
3 January	1982	1½p	20p	£165m (1)	8.1	148.1	144.8	144.1 (2)

(a) = Milk price increase

(b) = New price

(c) = Extra revenue generated

(d) = Percentage increase

(e) = Cumulative percentage increase

FOOTNOTES

(1) For a full year

(2) To September 1981 only.

TABLE IA

			MILK PRICE CHANGES			RPI	AVERAGE EARNINGS
DATE	(a)	(b)	(c)	(d)	(e)		
November 1978	-	13½p	-	-	100	100	100
3 June 1979	1½p	15p	£120m	11.1	111.1	108.4	110.8
17 February 1980	1½p	16½p	£ 77m	10.0	122.2	122.8	122.9
10 August 1980	½p	17p	£ 23m	3.0	125.9	132.5	137.0
4 January 1981	1½p	18½p	£165m	8.8	137.0	136.9	142.0
3 January 1982	1½p	20p	£165m (1)	8.1	148.1	154.4	155.5 (2)

(a) = Milk price increase

(b) = New price

(c) = Extra revenue generated

(d) = Percentage increase

(e) = Cumulative percentage increase

FOOTNOTE

(1) For a full year

(2) To September 1981 only

TABLE II

Confidential

MONTHLY RPI INCREASES IN 1981

ALL ITEMS INDEX (January 1974 = 100)

		Increase
January 1981	277.3	+ 0.6%
February "	279.8	+ 0.9%
March "	284.0	+ 1.5%
April "	292.2	+ 2.9%
May "	294.1	+ 0.7%
June "	295.8	+ 0.6%
July "	297.1	+ 0.4%
August "	299.3	+ 0.7%
September "	301.0	+ 0.6%
October "	303.7	+ 0.9%
November " (1)	306.5	+ 1.0%
December " (2)	309.6	+ 1.0%
January - March 1982 (2)	319.0	+ 3.0% (quarterly increase)

FOOTNOTES

(1) Estimate

(2) Forecasts

Ref: PO613

CONFIDENTIAL

PRIME MINISTER

LIQUID MILK PRICES

E(81)128

BACKGROUND

In E(81)128 the Minister of Agriculture, Fisheries and Food recommends an announcement before Christmas that the maximum retail price of milk will be increased in England, Wales and Northern Ireland by 1½p to 20p a pint from 3 January 1982; that the present premiums on Channel Islands and sterilised milk should be increased at the same time by ½p a pint; and that changes, broadly as recommended by Binder Hamlyn, should be made in the distributive costing system and in the dairy trade's target rate of profit.

Binder Hamlyn proposals and amount of price increase

2. The Committee agreed on 19 March (E(81)11th Meeting) that the present system of liquid milk price controls, whereby the Government set the maximum wholesale and retail prices, should be continued subject to implementation where practicable of Binder Hamlyn's report on the milk costing system. The Minister of Agriculture, Fisheries and Food proposes the introduction of a revised costing system incorporating nearly all Binder Hamlyn's recommendations. This would apply from October 1980 and as a result the trade will lose about £40 million which would have been due to them under the old system. He further recommends that for the retail part of the trade the target rate of profit should be 2 per cent on turnover and expressed as 0.66p a litre. This would be updated annually by reference to changes in milk prices with reviews at 3-yearly intervals. The Minister of Agriculture, Fisheries and Food, supported by the other Agriculture Ministers, regards the negotiation of this package with the dairy trade as a success. He will argue that anything more rigorous could lead to the breakdown of the present control system with the risk that milk prices would soar and that door-step delivery of milk might be discontinued.

3. He proposes that the retail price should be raised by 1½p per pint to 20p with effect from 3 January 1982 (compared with 13½p when the Government took office). This increase of 8 per cent would add to the Retail Price Index about 0.15 percentage points. The wholesale price would go up to 18.13p per litre from 1 January. Of the 1½p retail increase, 0.4p would go to the distributors and 1.1p to the producers in 1981-82. The Agriculture Ministers regard this increase as essential to raising producer incomes - see paragraphs 4 and 5 of E(81)128.

4. Treasury officials were first sent the detailed figures and proposals on 2 December and while they accept the broad thrust of Binder Hamlyn's recommendations they are not content with a number of important details. They believe that the calculations could allow too high a return, in terms of capital employed, to the dairy trade; in part because of the particular way in which the CCA depreciation charge is calculated. They do not agree that the target rate of profit, initially set at 0.66p per litre, should be indexed for 3 years. They do not think it necessary to increase the price, to the extent proposed by the Agriculture Ministers, to help milk producers' incomes. This leads them to call for some modification to the proposals, and to the accompanying draft statement, and to recommend an increase in the retail price of 1p rather than 1½p. The Chief Secretary will speak to these points.

5. The Minister of Agriculture, Fisheries and Food may well argue that, while it is possible to criticise some particular points in the proposals, they should be seen as a package which has been successfully negotiated with the trade. You will not want the Committee to get into any detailed discussion of the methodology of the Binder Hamlyn proposals, but the technicalities are important: they will have an effect on milk prices not only in January but later and the new system must be introduced on a firm footing. Even if it were possible for the Committee to decide on the January 1982 price increase on the information before them, you might ask the Minister of Agriculture, Fisheries and Food and the Chief Secretary to look further at the details of the system with the aim of reaching agreement on what should be said in the statement.

Timing of implementation and of announcement.

6. The Minister of Agriculture, Fisheries and Food discusses in paragraph 7 of E(81)128 your view that there should be no increase in the retail price before the school holidays are over. You will wish to consider his view that in practice housewives do not spend more on milk in the school holidays. He points out that the changes were made at the corresponding time in 1977, 1978 and 1981 and that the delay of a week would lose the industry £3 million in revenue.

7. Whether the increase is to be on 3 January or 10 January the Minister would wish to announce it, and his proposals on the Binder Hamlyn report, before the Recess. This has been the practice with previous increases in the price, and is particularly necessary for the introduction of the new system.

European Community Aspects

8. The year on year price increase proposed (8 per cent) is less than the increase in the milk target price (9 per cent) agreed at the 1981 price fixing. The Chancellor of the Exchequer might argue that we should be looking ahead to restraint at the 1982 price fixing and demonstrate this approach with a much more stringent price increase now. Against this it can be argued that the price set for liquid milk is not directly related to the Community price, which is of immediate significance only for butter and skim milk powder. The main concern may be to separate the announcement of the liquid milk price increase from the Community negotiations: the present proposals would do this.

9. There remains the longer term prospect that milk imports could damage the UK pricing arrangements. A case in the European Court may result in a relevant judgement in mid-1982.

HANDLING

10. After the Minister of Agriculture, Fisheries and Food has introduced his paper you will wish the Chief Secretary, Treasury to speak. The

other Agriculture Ministers will then want to comment - the Secretaries of State for Wales, Northern Ireland and Scotland (as explained in paragraph 9 of E(81)128 the arrangements in Scotland will be somewhat different, though they will take account of the increases elsewhere). The Secretary of State for Employment will want to comment on the timing of the increase and of its impact on the RPI.

11. It may well be that further work by the Ministry of Agriculture and the Treasury will be necessary and that the Committee will not be able to come to a final view until their meeting on Thursday 17 December. Subject to this, the main points with which you will wish to deal are:-

(i) The Binder Hamlyn recommendations.
- You will wish to ask the Minister of Agriculture, Fisheries and Food and the Chief Secretary, Treasury to reach agreement on the details.

(ii) The amount of the retail price increase.
- The effective choice seems to be between 1p and 1½p.

(iii) The timing of any increase in the retail price.
- 3 January or 10 January?

(iv) Whether the premiums on Channel Islands and sterilised milk should be increased by ½p per pint.
- The argument in paragraph 8 of E(81)128 is that this is necessary to ensure sufficient production to meet consumer demand.

(v) The timing of the announcement to the House of Commons.
- This should be before Christmas but there are no overriding technical reasons why it should not be after 17 December.

CONCLUSIONS

12. You will wish to sum up with reference to the 5 questions listed above. If possible, any outstanding points on the Binder Hamlyn changes should be settled bilaterally between the Minister of Agriculture, Fisheries and Food and the Chief Secretary, Treasury. There seems no reason why agreement should not be reached on the timing of the increase; if, because of disagreement over the underlying facts, agreement cannot be reached on the amount, the Committee will need to consider this further at their meeting on 17 December.

PG

P L GREGSON

9 December 1981

CABINET OFFICE
E 0288
9 DEC 1981
FILING INSTRUCTIONS
FILE No. ....

CONFIDENTIAL

1. MR WRIGHT
2. MR SCHOLAR

cc Mr Gregson

LIQUID MILK PRICES: E(81)128

The Economic Strategy Committee is due to discuss this paper after Cabinet tomorrow morning. For the reasons given below it is likely that it will be difficult to reach a final decision tomorrow and that discussion might have to be resumed at the meeting of E planned for Thursday 17 December. It would therefore be better to postpone discussion until the 17th when the other item on the agenda at the moment is Transport subsidies. If, however, it is necessary to take papers on British Aluminium on the 17th, and not earlier, I think it would be better to make as much progress as possible with milk tomorrow.

2. The difficulty arises because Ministry of Agriculture officials held their first discussion with the Treasury on the figures only yesterday and there is a further meeting today. The Treasury are not yet satisfied on the detailed proposals emerging from the Binder Hamlyn Report and, on present form, they are likely to argue for a 1p increase in the retail price rather than $1\frac{1}{2}$p. They would like a Treasury Minister to put in a paper on this. Discussion on these points tomorrow could, therefore, be confused and inconclusive; although a decision could be taken on whether the increase, at whatever level, should be on 3 January as the Minister of Agriculture wishes or after the school holidays as proposed by the Prime Minister.

3. The Minister of Agriculture still wants his paper discussed tomorrow so that he can make a statement as soon as possible. Provided firm decisions were taken on 17 December it would, however, be possible for him to make a statement before the Recess and to implement the increase in the price as early as 3 January if that were the Committee's decision.

CONFIDENTIAL

4. Provided there is room for it on the 17 December agenda, the safer course is to defer discussion of the milk paper until then.

D J L MOORE

9 December, 1981

CONFIDENTIAL

10 DOWNING STREET

From the Private Secretary

7 December 1981

Binder Hamlyn & Liquid Milk Prices

Thank you for your letter of 4 December. Thank you, too, for your letter of 3 December to Michael Alexander.

The Prime Minister would be grateful for a table showing all the increases in the retail price of milk since May 1979, giving dates of the price increases, the total cash increase in each instance together with the cumulative percentage increase. She wishes to set this table alongside a table of the monthly RPI increases in 1981, and in prospect, so as to consider what would be the best time for the increase to take effect.

I am not copying this letter as in our earlier correspondence.

MCS

Miss Kate Timms,
Ministry of Agriculture, Fisheries & Food.

CONFIDENTIAL

(2)

Prime Minister

I have told them that you do not wish there to be any increase in prices before the schoolchildren return to school in January.

MS 4/12

Michael - Pay!

Have a table of all increases in retail price of milk since May 1979 including ~~%~~ % increase of each, ~~cost~~ increase & the cumulative % increase in our time. Can I also have a 1981 monthly RPI increase table - so we can look at the last time for this increase etc.

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's Private Office

CONFIDENTIAL

Michael Scholar Esq
10 Downing Street
London SW1

4 December 1981

Dear Michael,

BINDER HAMLYN AND LIQUID MILK PRICES

You told me this morning that the Prime Minister wished to have a collective discussion of the proposals made by Mr Walker to his colleagues on implementing the recommendations of the Binder Hamlyn Report, and on the retail price of milk. We are urgently following up the possibility of a discussion in E Committee, where milk prices have previously been discussed. Mr Walker is anxious that this discussion should take place as soon as possible, in view of the very considerable pressure from the dairy trade for an early announcement on a package of measures.

In preparation for this meeting, for which we shall be circulating a paper, you may care to have a copy of my Minister's letter and enclosures of 2 December to the Chancellor of the Exchequer.

I am copying this letter to David Wright, who already has a copy of our letter of 2 December.

Yours sincerely
Kate

Miss V K Timms
Principal Private Secretary

CONFIDENTIAL

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

From the Minister

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1P 3HE

2 December 1981

Dear Geoffrey

BINDER HAMLYN: LIQUID MILK PRICES

As you know, following the two reports we had from Binder Hamlyn in February and October last year, I commissioned a further study from them on the feasibility of devising a more objective way of determining the target rate of profit on the lines they had suggested in their second report. I have received their report on this further study and enclose a copy of it.

As you will see, its recommendations have come as a great shock to the milk distributors, since they involve a very large cut in the target rate of profit available to them. It has been touch and go whether they could be prevailed upon to continue to co-operate in the price control system on this basis, but I am glad to say that they are now with great reluctance prepared to do so. Had they not been, it would have been very difficult to carry on with retail price control, and the retail price of milk could have soared in a way which would not only have added greatly to the Food Price Index but would have put at risk the continuation of doorstep delivery of milk.

We now need to take all the decisions necessary to implement a revised milk costings system. We also need to decide on future maximum retail and wholesale prices, following our autumn review. The wholesale price paid to the Milk Marketing Boards should have been increased on 1 October (it was actually reduced on 1 April for the summer season), and I have been under heavy pressure to declare our intentions at a time when dairy farmers are themselves in considerable economic difficulty. I am sure it was right to defer this until we could sort out the future system for distributive costings, but any further delay would be impossible to defend, and we must clearly take our decisions and announce them as quickly as possible.

I enclose a draft statement which sets out the changes I propose to make to the costings system in implementation of the Binder Hamlyn recommendations and the decisions I propose on prices.

As regards the review of the costings system, I am proposing to accept virtually all of the detailed recommendations of Binder Hamlyn with only a few insignificant exceptions. On the central question of the target rate of profit I propose to accept the method proposed by Binder Hamlyn for establishing the basic target rate and to drop the existing depreciation convention as they suggest.

Of the two alternatives they offer, I propose to adopt the CCA depreciation proposal which gives the greatest reduction in the target rate of profit (the margin saving from change in depreciation convention being a much less stable and predictable figure). I propose also, despite very strong contrary representations from the Dairy Trades Federation, to follow Binder Hamlyn's strong preference for the use of preselected reference groups and of a straight average. When I sought their comments on the latest Binder Hamlyn report, the DTF argued strongly that, for the retail part of their industry, the reference group proposed by Binder Hamlyn was seriously unrepresentative of retail activity and that it ought to be further refined to eliminate this source of distortion or the average should be struck on a weighted basis, which would raise the rate of profit on turnover in the reference group from 2.0% to 2.7%.

Although I considered there was some justice in their arguments, I shared the view of Binder Hamlyn that it would be difficult to find a satisfactory and objective way of further adjusting the retail reference group and, having taken account also of the Binder Hamlyn arguments about the lower degree of risk in the dairying industry, I have concluded that we should base the basic target rate of profit on the bottom of the bracket (2.0-2.7%) established by Binder Hamlyn. This conclusion has been accepted only with very great reluctance by the DTF.

The effect of this will be to reduce the basic target rate of profit to 0.66 ppl compared with the existing figure (established two years ago and not uprated while the full operation of the costing system has been suspended) of 0.90 ppl. In accordance with the recommendations of Binder Hamlyn I propose that this new basic rate should be updated annually in line with the movement of the milk price and reviewed every three years or so in a fresh comparison exercise.

I propose to introduce the revised costing arrangements at the earlier possible moment, ie with effect from 1 October 1980. This means that they will be fed into the usual autumn costings exercise that is now getting under way. I am also proposing, and again this has been accepted exceedingly reluctantly by the Dairy Trade, that the outstanding shortfalls in margin arising under the old costing conventions before that date should be written off: these amount to £40 million.

As regards milk prices, I propose that the retail price should be increased on 3 January 1982 by 1½p/pint to 20p/pint. This will be a full year after the previous increase and represents an increase of 8%. This is significantly below the forecast rate of increase in the RPI in that period and should not cause a significant depression in the trend of liquid milk consumption. I hope it will be possible to avoid any further increase in the retail price for at least the greater part of 1982. Taking account of this increase in the retail price and of the effects of implementing the Binder Hamlyn recommendations I propose to increase the wholesale price in England, Wales and Northern Ireland with effect from 1 January 1982 to 18.130p/litre.

The effect of this will be to provide some increase in the returns of milk producers but not to a level which would stem the continual erosion in the real value of their net margins which has now continued unabated since 1977/78. They have been pressing me for several months to take early action to restore the real value of their net margin at least to last year's level. Now that we have completed the review of the costings system I have no grounds for deferring a retail price increase any longer and for the reasons I have explained I think this cannot be less than 1½p/pint.

I have asked my officials to get in touch with yours and their opposite numbers in the other Departments concerned so that we can provide any further information necessary about the technical details involved in all this. I hope that on this basis my colleagues will be able to give their early agreement that I should make a written statement on the lines I propose.

I am sending copies of this letter to John Biffen, Humphrey Atkins, George Younger, Jim Prior, Nicholas Edwards and Sir Robert Armstrong.

PETER WALKER

Confidential

Draft statement by the Minister of Agriculture

Liquid milk prices: review of the milk costings system

On 16 April 1981 I made an interim statement about the review which has been undertaken by an independent firm of accountants, Binder Hamlyn, of the way in which the dairy trade's costs are measured and taken into account under the system of control of maximum prices for liquid milk. I indicated that the Government accepted the need for certain detailed changes in the costings arrangements and in particular that we accepted Binder Hamlyn's two major recommendations: - that wholesale sales should be included within the costings system; and that it would be right in principle to determine the dairy trade's target rate of profit by reference to an objective and realistic comparison with rate of return in other industries.

In their second report of October 1980 Binder Hamlyn outlined a possible method of doing this based on return on capital but concluded that only a further detailed study would show whether this method was feasible in practice. I therefore commissioned them to carry out such a study and I have now received their report on this.

This report recommends that a basic target rate of profit for the dairy trade should be established on the basis of comparisons with two similar groups of industries. For the processing part of the dairying industry it recommends a comparison with the rate of return on capital in a specified reference group of food manufacturers: for the retail part the comparison would be with the rate of profit on turnover in a specified group of food retailers. Binder Hamlyn recommended that the current convention on depreciation (which allows writing off in one year on the basis of tax allowances) should be changed and replaced by one on a basis consistent with the calculation of the reference rates of profit. They proposed that this should be done on the basis either of a historic costs depreciation charge or alternatively an estimate of current cost accounting (CCA) depreciation charge could be made by scaling up the historic cost charge and a corresponding reduction would then be made to the calculated target rate of return. Binder Hamlyn recommended that the basic target rate of profit thus established should be uprated annually either on the basis of the Retail Price Indix or by reference to changes in milk prices with a full review of the target rate of profit at less frequent, preferably 3 yearly, intervals.

The Government has decided to accept these recommendations and virtually all the other detailed recommendations of Binder Hamlyn (which are listed in the annex to this statement). The target rate of profit will be determined on the basis of a CCA depreciation charge and updated by reference to changes in milk prices. The new costings conventions will be effective from 1 October 1980 and will therefore be taken into account in the current autumn costing review which is now getting under way.

In making these changes to the milk costings system it has been my objective to encourage the provision of a full and efficient service to consumers, especially through the maintenance of a viable doorstep delivery system, and the continued health and competitiveness of the dairying industry and of the milk production industry which depends to so large an extent on returns from the liquid milk market. I have paid particular attention to shaping the costings system in such a way as to maximise the spur to efficiency it provides, both through the incentive to beat the average which Binder Hamlyn recognised it to contain, and by such measures as the removal of persistent loss makers from the sample and the use of simple averages. I am confident that the revised system, incorporating as it does, virtually all the specific recommendations of Binder Hamlyn, is well adapted to this end.

I recognise that the need to carry out this fundamental and thorough review of the costings system has inevitably created a period of uncertainty and some delay in initiating the usual autumn review of costings and prices; and that both these important industries can reasonably now look for a period of greater stability and regularity in the operation of the system so that they have a firmer basis for planning their commercial operations over the year as a whole. It will be my intention in operating the revised price control and costing system to seek to provide that firmer basis and to contribute to the fullest possible extent to the achievement of the objective I have stated above.

Having assessed the effect which the implementation of the changes to the costings system recommended by Binder Hamlyn will have upon the measured level of costs and profits in the dairy industry, the Government has also given consideration to the levels of the maximum prices for milk to apply this winter. It has decided to increase the maximum retail price for ordinary pasteurised milk by 1½p per pint, to 20p per pint, on 3 January 1981.

The maximum retail price for farm-bottled milk will be increased by just ½p per pint to bring it into line with the price for ordinary pasteurised milk, in accordance with the decision announced on 1 December 1980.

In order to reflect the increases in the maximum retail prices, and taking account of the changes in the measured levels of dairies costs and profits arising from the implementation of Binder Hamlyn's recommendations, the maximum wholesale prices of milk in England, Wales and Northern Ireland will be increased as follows with effect from 1 January 1982:

	Present Price (p per litre)	Increase (p per litre)	Price from 1/1/82 (p per litre)
England & Wales (except London)	16,200	1.930	18.130
London	14.563	1.800	16.363
Northern Ireland (except Belfast)	18.840	1.930	20.770
Belfast	18.749	[2.011]	[20.770]

Orders giving effect to these changes will be laid before Parliament as soon as possible.

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2 December 1981

Summary of Binder Hamlyn Recommendations and Decisions Taken on Them

This annex lists all of the recommendations which were contained in the three reports by Binder Hamlyn, dated February and October 1980 and November 1981. For each recommendation, the annex lists the action which the Minister of Agriculture, Fisheries and Food intends to take, following his discussions with the Dairy Trade Federations, Milk Marketing Boards and Farmers' Unions in England, Wales and Northern Ireland.

Recommendation	Intended Action
I. SCOPE OF THE COSTINGS SYSTEM	
1. All milk sales (including wholesale sales) by costed dairies should be fully included in the costings system, with discounts given on wholesale and semi-retail sales also being included in the costings.	1. Agreed.
2. Discounts given to bottled milk buyers (ie wholesale sales) and to shops should be monitored and, if excessive, limited in the costings.	2. Agreed.
3. Monitoring and limitation of discounts given to bottled milk buyers should be by reference to a triennial costing of a small sample of bottled milk buyers.	3. Agreed in principle. A further study is needed to establish how best to cost bottled milk buyers.
4. Monitoring and limitation of discounts given to shops should be by reference to published data about gross margins earned by general food retailers.	4. Agreed.

II THE COSTINGS SAMPLE

5. Although difficult to achieve at present, there could be advantage in there being one UK sample.	5. Different arrangements now apply in Scotland, but a single sample for E, W and NI is to be established.
6. The sample should be structured so as to include costees which in terms of throughput are representative of the trade overall; the representation of smaller dairies should be increased.	6. Agreed. The proposed new sample takes account not only of throughput, but also of geographical location and type of ownership. The representation of smaller dairies will be increased.
7. New costees should continue to be selected by agreement between MAFF and the DTFs, but participation by selected costees in the sample should be made compulsory.	7. The DTFs will use their best endeavours to persuade selected costees to participate. The Minister reserves the right to introduce compulsion, if necessary.

III GEOGRAPHICAL ALLOWANCES

8. On the evidence available at the time, Binder Hamlyn were unable to take a firm view on the need for a Special London Allowance in the long-term.	8. It is now apparent that costs are higher in London than in the provinces. An allowance will be paid but calculated using a simplified and objective method.
9. The London Distributive Allowance should be restricted to a fixed proportion of the Special London Allowance.	9. The London Distributive Allowance will be set at 40% of the Special London Allowance.

10. If there continues to be a difference in costs between Belfast and other areas then, subject to Government policy the Belfast Allowance should be continued.	10. For decision by the Secretary of State for Northern Ireland.

IV COST CONVENTIONS

11. Continue to calculate deduction for cost of "other" goods sold on rounds but review formula and figures.	11. New formula and provisional figures agreed.
12. Continue proprietors' remuneration formula with minor modifications.	12. Agree to continue, but reserve judgement on need for modification.
13. Allow costs of rounds shortages to be included subject to maximum level	13. Agreed.
14. Roundsmen's commission on milk sales should continue to be allowed in full, but that for other goods excluded.	14. Agreed.
15. Continue to exclude interest payable and receivable from the costings.	15. Agreed.

V TARGET RATE OF PROFIT AND DEPRECIATION

16. The basis of the depreciation charge in the costings must be consistent with the basis of the target rate of profit.	16. Agreed.
17. The present system of using tax allowances and net rateable values to represent the cost of depreciation in the costings should be replaced by the use of an actual charge on either a historic or CCA basis.	17. Agreed. A depreciation charge on a CCA basis will be used.

18. The target rate of profit for milk processing and wholesale sales should be calculated as a rate of return on capital employed by reference to a selected group of food manufacturing companies.	18. Agreed.
19. The target rate of profit for milk retailing should be calculated as a rate of profit on sales by reference to a selected group of food retailing companies.	19. Agreed.
20. The simple average should be used to calculate the appropriate reference rates of return on capital or turnover from the reference groups.	20. Agreed.
21. The lower degree of risk in the dairy industry should be taken into account in fixing the target rate of profit.	21. No specific adjustment made, but target rate agreed upon in lowest of possible range recommended by Binder Hamlyn.
22. The target rate of profit for 1980 should be 0.81 ppl with historic cost depreciation, or 0.66 ppl with CCA depreciation.	22. Agreed to use 0.66 ppl with CCA depreciation.
23. There should be a full review of the target rate of profit every three years but, in the meantime, the TRP should be updated by reference either to the RPI or to increases in milk prices.	23. Agreed. Updatings will be by reference to increases in the milk price.

VI THE AVERAGING METHOD	
24. The median or the simple average should be used.	24. Agreed to use simple average.
VII COST COLLECTION SYSTEM	
25. Simplify forms and instructions.	25. Agreed. This work is in progress.
26. Clarify and define role of investigating accountants.	26. Agreed. Discussions in progress.
27. Reorganise staff in London and Belfast.	27. Still to be considered in light of final decisions on future system.
28. Consider use of computers and self-assessment.	28. Cost-benefit study of use of computers in hand.
VIII MARGIN CALCULATION	
29. Pilot costings should be replaced by use of cost indices in making projections of future distribution margin requirements.	29. Decided that pilot costings satisfactory; cost indices would be marginally cheaper to operate but would be less accurate and more complex.
30. Retrospective adjustments should be made only if they exceed a certain percentage of the TRP.	30. Agreed. Adjustments to be made only if greater than 5% of TRP.
31. BH changed their original recommendation and concluded that the penny schedule to be adopted would depend upon the details of the costings system finally agreed.	31. A formula for penny schedule factor has been agreed, with the approval of BH.
IX EFFICIENCY	
32. Use of the simple average will ensure that the distributive margin is based on the results of the "reasonably" efficient dairy.	32. Agreed.

33. A further incentive to efficiency could be provided by basing the average on the very efficient dairy.	33. Not reflected in the averaging method chosen. but loss-making costees will be eliminated from the sample.

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2 December 1981

CONFIDENTIAL

20

10 DOWNING STREET

From the Private Secretary

4 December, 1981.

Milk Prices

As I told you on the telephone this morning, the Prime Minister has had a further look at your Minister's letter to her of 27 November.

The Prime Minister would like the proposed increase in the retail price of liquid milk to be discussed by Ministers collectively, and I understand that you have begun to set this in motion in consultation with the Cabinet Office.

The Prime Minister has also commented that she hopes there will be no question of an increase in the price of milk before the schools return in January.

I am sending copies of this letter to John Kerr (HM Treasury), Richard Dykes (Department of Employment), and Peter McCarthy (Department of Trade)

M. C. SCHOLAR

Miss Kate Timms,
Ministry of Agriculture, Fisheries and Food.

CONFIDENTIAL

20

CP

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the Minister's Private Office

CF x please
MES.

Michael Alexander Esq
Private Secretary
10 Downing Street
London SW1

3 December 1981

Dear Michael,

You spoke to me this afternoon about reports from the Press Association that my Minister was shortly to announce an increase in the retail price of milk to 20p per pint, an increase of 1½p. I explained to you that such a story could only be speculation at this time, but that, as foreshadowed in my Minister's letter x to the Prime Minister on the Food Price Index dated 27 November, we were making proposals to colleagues for implementation of the Binder Hamlyn recommendations and on the retail milk price from January 1982. The Minister has asked me to say that the negotiations he has conducted with the National Farmers' Union, the Milk Marketing Board and the Dairy Trade Federation over the last three or four weeks have been conducted in strict confidentiality, which has been observed by all parties to the discussion. He is therefore most concerned that a leak of information appears to have occurred immediately after he has put his proposals to his colleagues, as he did in a minute dated y 2 December.

I am copying this letter to John Rhodes, Stephen Gomersall, Muir Russell, Steven Boys Smith, John Craig and David Wright.

This went to colleagues on the OD(E) net, not to the Prime Minister.

Yours sincerely
Kate

KATE TIMMS
Principal Private Secretary

Prime Minister (2)

Y SWYDDFA GYMREIG
GWYDYR HOUSE
WHITEHALL LONDON SW1A 2ER
Tel. 01-233 3000 (Switsfwrdd)
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Oddi wrth Ysgrifennydd Gwladol Cymru

The Rt Hon Nicholas Edwards MP

MLS 4/12

WELSH OFFICE
GWYDYR HOUSE
WHITEHALL LONDON SW1A 2ER
Tel. 01-233 3000 (Switchboard)
01-233 6106 (Direct Line)

From The Secretary of State for Wales

CONFIDENTIAL

3rd December 1981

Dear Geoffrey

BINDER HAMLYN: LIQUID MILK PRICES

The proposals set out in Peter Walker's letter to you of 2 December represent, in my view, the best possible compromise between the various interests, and indeed it is a remarkable achievement by Peter to have got agreement after long and difficult negotiations.

The agreement now on offer with the DTF is the most we can expect them to accept.x Equally there can be no question of the need of the milk producers for a significant price increase. I have been for some time under considerable pressure from Welsh farmers about the state of the dairy industry and I am certain that the increase in producer returns which a $1\frac{1}{2}$p retail price increase will permit is the minimum response we can reasonably make.

I therefore thoroughly support Peter's proposals and I very much hope that you will give them your early agreement.

I am copying this to the recipients of Peter's letter.

Yours ever
Nick

x and indeed more than we could have dared to expect

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
Treasury
Parliament Street
LONDON

CONFIDENTIAL

10 DOWNING STREET

From the Private Secretary

30 November, 1981

The Prime Minister was grateful for your Minister's letter of 27 November about the latest forecasts of changes in the Retail Food Price Index.

She has carefully noted the points in your Minister's letter.

I am sending copies of this letter to John Kerr (HM Treasury), Richard Dykes (Department of Employment), and Peter McCarthy (Office of the Minister of State for Consumer Affairs).

M. C. SCHOLAR

Miss Kate Timms,
Ministry of Agriculture, Fisheries and Food.

CONFIDENTIAL

CONFIDENTIAL

Prime Minister

(2)

c JV
AD

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD
WHITEHALL PLACE, LONDON SW1A 2HH

MCS 27/11

From the Minister

The Rt Hon Margaret Thatcher MP
10 Downing Street
London SW1

27 November 1981

Collective Discussion
Background

My Prime Minister

I am writing to report on our latest forecasts of changes in the Retail Food Price Index (RFI).

When I wrote to you in August the annual rate of increase in food prices was in the region of 8%. Since then a number of factors have emerged due principally to the prices of seasonal foods, especially the recovery of potato prices, which have resulted in the October figure published last Friday showing an annual increase of 9%, and I believe that the prospects for the period between now and March are that the rate will be between 9% and 10%.

Included in this projection is the assumption that there will be an increase in the retail price of liquid milk in January. I have, in spite of considerable pressure, provided no increase in the liquid price since the last liquid price announcement last December, and I have used Binder Hamlyn as an excuse to delay any announcement. By this means, when an increase is given in January it will be the first increase for a year and I hope an increase below the rate of increases of food prices during the past year. I shall of course be putting proposals to my colleagues.

Prices of imported materials purchased by food manufacturers in the third quarter were running at 13% above a year earlier, reflecting the exchange rate depreciation, and I am afraid that average earnings for those employed in food manufacturing in August were 15% higher than a year before and the distributive trades 12% higher. Naturally I hope that a lower pattern of wage settlements in the coming year will assist us in keeping down prices during 1982.

CONFIDENTIAL

I am copying this letter to the Chancellor of the Exchequer, the Secretary of State for Employment and the Minister of State (CA), Department of Trade.

Yours ever

PETER WALKER

Agriculture.

Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

1 Mr Pattison
2 PA

WR 23/7

From the Minister's Private Office

W Rickett Esq
10 Downing Street
London SW1

23 July 1981

Dear Willie,

In your letter of 6 July to Peter Shaw on school milk, you mentioned that the Prime Minister had wondered whether it was presentationally wise to transfer this function to the Intervention Board at a time when the Board's operations are hampered by industrial action.

It is of course to be hoped that the Government's most recent pay offer will result in an early return to normal working, but, even if this were not the case, a problem would only arise in practice when the Board came to make payments under the new scheme. In view of the time needed for claims to be submitted and processed, such a situation is unlikely to occur until October at the earliest; and, given that any delay in transferring administrative responsibility to the Board would effectively mean further delay in introducing the new scheme, my Minister is satisfied that the current industrial action does not constitute an overriding objection and that the transfer of responsibility should now go ahead. He is therefore proposing to make today a written Parliamentary statement along the lines attached to the minute which the Secretary of State for Education sent to the Prime Minister on 1 July.

I am copying this letter to the recipients of yours.

Yours sincerely

Kate.

Kate Timms
Principal Private Secretary

JFH

Agriculture.

CF

10 DOWNING STREET

From the Private Secretary

6 July 1981

Dear Peter

The Prime Minister was grateful for your Secretary of State's minute of 1 July on school milk. He sought her approval for transferring to the Minister of Agriculture responsibility in England for the EC scheme for subsidising milk and milk products supplied to children in schools.

The Prime Minister has noted that, under the new arrangements, the scheme will be administered in the UK by the Intervention Board for Agricultural Produce . She wonders whether it is presentationally wise to transfer a function to the Intervention Board when the Board's operations are hampered by industrial action. However, if Mr. Walker is satisfied that this is not an overriding objection, the Prime Minister is content for the transfer of responsibility to go ahead.

I am copying this letter to the Private Secretaries to the Chancellor of the Exchequer, the Minister of Agriculture, Fisheries and Food, the Secretaries of State for the Environment, Scotland, Wales and Northern Ireland and to Sir Ian Bancroft and Sir Robert Armstrong.

Yours

Willie Rickett

Peter Shaw, Esq.,
Department of Education and Science.

HL

Prime Minister 1

I have asked MAFF for advice on whether it is wise presentationally to transfer a function to the Intervention Board for Agricultural Produce when the Board is crippled by industrial action. Are you content subject to satisfaction on this presentational point?

[initials] 3/7

SECRETARY OF STATE FOR EDUCATION AND SCIENCE

PRIME MINISTER

Yes

SCHOOL MILK

I am currently responsible in England for operating the European Community scheme for subsidising milk and milk products supplied to children in schools. By agreement with the Minister of Agriculture, I seek your approval for transferring this responsibility to him.

Background

2. The scheme was introduced in 1977, when local education authorities were under a duty to provide free school milk to 5-7 year olds and certain other categories of pupil. That duty was removed by the Education Act 1980, and, as a result, the dairy industry expressed concern that consumption of school milk would fall. The Minister of Agriculture has therefore negotiated and agreed revised arrangements with the European Commission which will allow local authorities to buy milk directly from the dairies at net-of-subsidy prices. At present they claim termly in arrears.

3. Other changes in the eligibility rules for the scheme are designed to make it easier for individual authorities to sell subsidised milk in schools. The new arrangements should not involve any increase in local authority or Exchequer expenditure. The Chancellor of the Exchequer is content.

Reasons for Transfer

4. The education departments in the United Kingdom accepted responsibility for administering the scheme when it was introduced. The transfer is proposed for the following reasons:-

a. the Education Act 1980 has greatly diminished my policy interest in school milk; in particular, I have no policy interest in promoting school milk sales;

b. the scheme is primarily an instrument of agricultural policy; the change will therefore bring together responsibilities for policy and administration;

c. the Minister of Agriculture has general responsibility for dealing with the European Commission on matters of agricultural policy and will be taking the lead in a forthcoming Commission review of the subsidy scheme as a whole.

Other Points

5. The scheme will be administered in the United Kingdom by the Intervention Board for Agricultural Produce. It is only in England that a transfer of Ministerial function is involved; elsewhere, the territorial Secretaries of State are responsible for agriculture as well as education.

6. There are no significant manpower implications arising from the transfer of responsibility.

7. The function is non-statutory and the transfer can therefore take place administratively. If you are content, the Minister of Agriculture will announce the change in a Written Answer as part of a more general statement on the new arrangements. I attach a copy of the proposed statement.

8. I am sending copies of the minute to the Chancellor of the Exchequer, the Minister of Agriculture, Fisheries and Food, the Secretaries of State for the Environment, Scotland, Wales and Northern Ireland, Sir Ian Bancroft and Sir Robert Armstrong.

M.C.

MARK CARLISLE

1 July 1981

SCHOOL MILK

DRAFT ARRANGED PARLIAMENTARY QUESTION AND ANSWER

To ask the Minister of Agriculture, Fisheries and Food, if he is now in a position to make a statement about the arrangements for claiming European Community subsidy on school milk.

MR PETER WALKER

I am glad to say that agreement has now been reached with the European Commission on the revised arrangements which will help local authorities to sell milk in schools with the advantage of the subsidies available from FEOGA for school milk. The Commission have agreed that the contribution made by public authorities in the United Kingdom should be aggregated for the purpose of calculating the 25% national contribution required under the Community Regulation. They have also agreed that, while the price charged by local authorities for the milk should reflect the value of the Community subsidy, it may take account of the average costs incurred by local authorities in distributing it to schoolchildren. A circular letter explaining the new arrangements in detail is being sent today to local authorities.

With the agreement of the Prime Minister I am taking over from the Secretary of State for Education and Science responsibility for administering the scheme in England. Payments will now be made directly by the Intervention Board for Agricultural Produce using funds paid in advance by the European Commission. Parliamentary approval for this new service will be sought in a Supplementary Estimate in due course.

CONFIDENTIAL

Agriculture

PAC(81)6

MS

The Recent Adjustment on Milk Prices

It is hoped that this brief will be of some help to Members in discussing the Milk Price changes with farmers and their local NFO Branches.

INDEX

Conservative Research Department
32 Smith Square, London SW1

RBC/FL
1/5/81

THE RECENT ADJUSTMENT ON MILK PRICES

1. Introduction

On 16 April the Minister of Agriculture, Peter Walker, announced that for the summer months the distribution of the proceeds from the liquid milk market would be adjusted so that the Milk Marketing Board, on behalf of producers, would receive 16.2p per litre and the distributors, from the Dairy Trade Federation, would obtain 16.4p per litre.

It is vital to the milk producers that the doorstep delivery service is maintained. When, some years ago, such a service was allowed to collapse in Holland, liquid milk consumption went down by 21%. Over many years a system has operated to assess the cost of distribution by the dairy trade and to fix their share of the liquid milk price in accordance with those costings.

2. The Facts of the Situation

Peter Walker, Minister of Agriculture was the first Minister for 38 years to break that system because he did not consider that one can give an adequate return to the producers and continue the system that his predecessors had agreed with the dairy trade without charging a price to the consumer which would have resulted in a substantial drop in milk consumption.

He has therefore been tougher with the dairy trade than any of his predecessors, and had he continued the system as operated by his predecessors over these last two years, the dairy trade would have obtained £32 million more than they in fact have received.

The Minister appointed a firm of independent accountants, Binder Hamlyn, to examine in great detail the system operated towards the dairy trade and they came up with recommendations which are likely, when implemented, to result in a reduction in the receipts of the dairy trade estimated, by Binder Hamlyn, to be of the order of £25 million a year.

Peter Walker told the dairy trade and the milk producers that he intends implementing the basic proposals of the Binder Hamlyn Report.

During their period of office, this Government has increased the liquid price of milk by 37%, the maximum that the Minister considered was possible without substantially reducing liquid milk consumption. In fact since the last increase the Government made in January of 1½p per pint, there has been a 2% drop in milk consumption. It is not, therefore, possible for liquid milk prices to be increased without endangering the levels of consumption which in turn, of course, will endanger the returns to the producers.

Producers are now receiving on the liquid milk market 21.8% more than when we came into office. In addition to this, the three green pound devaluations, together with the recently announced increases in the price fixing of 9% on the target price for milk, will improve the receipts of producers from the manufacturing milk market. Currently there is a 3.8p per litre premium on the receipts that the farmer obtains from the liquid milk market as opposed to the manufacturing milk market.

The Government's policy of maintaining our green pound advantage gives a fundamental advantage to the dairy industry in both exporting to Europe and in obtaining a larger share of the United Kingdom market for British dairy products such as butter, cheese, yoghurt and other products.

Some of the criticism of the recent adjustment in the price gives the impression that it is unusual to reduce the producers' returns during the summer months. In fact, the Board normally dropped the producers' price in the Spring and put it up in the Autumn in order to take into account the seasonal variations in milk production costs. There is, therefore, nothing unusual or new in the Spring adjustment.

The Government have endeavoured to make a judgement in terms of distribution which will retain the doorstep delivery service, improve the potential of the dairy industry in manufactured goods and give the maximum available return to the producer.

If anybody wished to dispute the judgement as being unfair between the producers and the distributors it would be open to the producers, in the form of the Milk Marketing Board, to go to arbitration. The Government does not believe they will do this, and they have not indicated that they will do this, because they must recognise that the Government's distribution is fair and reasonable in the circumstances involved.

The dairy distribution system is highly labour intensive by its very nature, it is a substantial consumer of fuel, and therefore has been very substantially hit by the wage inflation and the rise in fuel costs over recent years.

Two encouraging signs as far as the producers are concerned are that, from the latest figures, the number of in-calf heifers is up nearly 2% on a year ago and the price of dairy cows is being very well maintained.

3. Conclusion

The Government's objective will be to continue to see that the producer has the benefits of a soundly based doorstep distribution system which is the envy of milk producers throughout the world, and an improving position in the manufacture and processing of dairy products.

Ref: A04490

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PRIME MINISTER

Liquid Milk Price Controls
(E(81) 30, 31 and 32)

BACKGROUND

At their meeting on 4th December the Committee invited the Minister of Agriculture, in consultation with other relevant Ministers, to arrange for an interdepartmental review of the recommendations in the Binder Hamlyn Report on the milk costing system, and of the Secretary of State for Northern Ireland's proposal for ceasing to control wholesale prices, and to make recommendations (E(80) 43rd Meeting, Item 3). The report by officials is circulated under cover of E(81) 30 and provides a detailed description of the present system, a summary of the Binder Hamlyn recommendations, and a discussion of the pros and cons of abandoning the present system of price controls in whole or in part. In E(81) 31 the four Agriculture Ministers advise that it would be "political and economic folly to dismantle the control system and thus bring about a free-for-all" and they recommend continuation of the present controls subject to implementation of the Binder Hamlyn recommendations, with some modification for Scotland and the reintroduction of a producer subsidy in Northern Ireland. The CPRS, in E(81) 32, summarise the main arguments and raise the question of whether, contrary to the views of the Agriculture Ministers, more fundamental changes should be introduced over a transitional period.

2. Under the present system the Government sets maximum wholesale and retail prices taking account of the average costs in processing and distribution as measured by independent accountants from representative samples and with allowance for a reasonable level of profit. The price maxima are reviewed twice a year. Since January the retail maximum has been 18½p a pint compared with 13½p when the Government took office. 1p on a pint adds to the Retail Price Index by about 0.1.

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3. The case put for controls, which date from the last war, is that in the absence of imported milk they protect the consumer from exploitation by the Milk Marketing Boards, which are monopoly sellers, and by the few relatively large milk distributors.

4. It is central to the Agriculture Ministers' judgment that in the United Kingdom, other than in Scotland, the doorstep delivery service would be at risk if controls were abandoned. In England and Wales the fixed costs of the service represent about 80 per cent of the total. It is feared that if, following decontrol, doorstep delivery prices were to rise relatively, and there were to be a switch to shop sales, unit costs of doorstep delivery would go up and the economics of the system could be undermined. The papers point out that the doorstep delivery system is very popular with consumers, other than in Scotland; important to milk producers in that it is held to sustain demand; and a source of employment to 45,000 people spread over the country.

5. On the other hand, as the papers by officials and by the CPRS bring out, it cannot be taken for granted that the removal of controls would have adverse consequences and lead to the break up of the doorstep delivery system:

(i) In Scotland doorstep delivery is available to 96 per cent of the urban population but 40 per cent do not use it, and neither consumption nor the delivery service has apparently suffered.

(ii) There is a lack of comprehensive information about the economics of milk distribution in Scotland and the rest of the United Kingdom and so the case cannot be proven either way.

(iii) It is by no means obvious that without controls distributors would cut their own throats by raising prices to a level which would wreck the doorstep delivery system.

(iv) There is competition with shops already and this is increasing in England and Wales with Sainsburys, for example, now selling carton milk at $1\frac{1}{2}$p per pint below the maximum.

(v) Further competition to doorstep delivery could come anyway from Continental "long life" milk if the European Court rule in early 1982 in favour of the Commission's challenge to the exclusion of imports by our domestic health and hygiene legislation and/or if there is Community agreement on harmonisation of hygiene regulations.

6. The Agriculture Ministers conclude, nevertheless, that since the consequences of removing the controls are unknown, and might very well be irreversible, they should be maintained in the interests of the consumer. They point out that the Director General of Fair Trading has now decided against a reference to the Monopolies Commission on the retail milk distribution arrangements in England and Wales; and that, although Binder Hamlyn were not considering the basic question of whether to abolish controls, they did conclude that the present system allowed for incentives to individual firms to operate efficiently and so beat the average.

7. The Agriculture Ministers recommend that the Binder Hamlyn recommendations for improving the costing system and setting the target rate of profit should be accepted, subject to further discussion between the Minister of Agriculture and the Secretaries of State for Scotland and for Trade on the precise application of the costing changes in Scotland (the Binder Hamlyn recommendations are discussed in more detail in paragraphs 13-20, and in the appendix, of the report by officials circulated with E(81) 30). If these changes are made it is estimated that they would lead to a saving of £25 million on the present total distribution margin of about £900 million and to 1p per pint off the retail price for $2\frac{1}{2}$ months. In other words the Binder Hamlyn report largely endorses the present methodology. If it was accepted, the total costs of administering the system would rise to about £540,000 a year of which £450,000 would represent fees to accountants.

8. It is further recommended, in paragraph 9 of the Minister's paper E(81) 31, that consideration should be given to reintroducing the public expenditure subsidy to Northern Ireland milk producers so as to assure them of a level of income comparable to that obtained elsewhere in the United Kingdom.

This is for further discussion between the Minister of Agriculture, the Chancellor of the Exchequer and the Secretary of State for Northern Ireland.

HANDLING

9. You will wish to invite the Minister of Agriculture to introduce E(81) 30 and 31 and to give each of the Secretaries of State for Scotland, for Wales and for Northern Ireland an opportunity to add their glosses. Mr. Ibbs might then speak to his paper (E(81) 32). The Secretary of State for Trade will wish to give his views on which course would best serve the interests of the consumer; the Chancellor of the Exchequer will want to comment on the financial and economic implications; and the Foreign and Commonwealth Secretary on whether the European Court ruling is likely to lead to our having to accept imported milk.

10. The first question for the Committee is whether they accept the advice of the Agriculture Ministers that the present system of controls should stand. Their case seems largely to rest on the fear that dismantling of the controls would be a leap in the dark, possibly leading to price increases and disruption of the doorstep delivery system for which the Government would be blamed. While there is some force in this argument, the Committee may feel that it is not sufficient to justify the view that dismantling would be "political and economic folly" and that there is also some force in the counter arguments listed in paragraph 5 above.

11. If the Committee is not fully persuaded by the case against removing controls, they might wish to follow up the CPRS's proposal for further work on the options listed in paragraph 44 of the officials' report E(81) 30 and with a view to more fundamental changes over a transitional period. The case for this turns significantly on the judgment, on which the Foreign and Commonwealth Secretary may be able to advise, of how likely it is that imports will continue to be excluded by United Kingdom health and hygiene regulations. If the reality is that milk will be imported in the next year or so, and at prices below our own maxima, this would reinforce the case for starting now with some transitional arrangements which would prepare the way and also avoid any

impression that our system had been suddenly overturned by a European Court ruling. In any event there may be a case for some further contingency work to assess the best response to imports and also the tactical question of whether we should work constructively towards the establishment of harmonised health and hygiene regulations or adopt an obstructive approach.

12. If, however, the Committee rule out radical changes immediately, they will wish to consider the proposals put forward by the Agriculture Ministers for implementing the Binder Hamlyn proposals, with suitable modifications in Scotland, and for considering the reintroduction of a producer subsidy in Northern Ireland. Since it is proposed that further examination of this should be undertaken by the Ministers directly concerned, it should not be necessary for the Committee to discuss these proposals in any detail.

CONCLUSIONS

13. In the light of the discussion you will wish to record conclusions:

Either accepting the recommendations in paragraph 10 of E(81) 31 for continuation of the present system subject to implementation of the Binder Hamlyn proposals with modifications in Scotland and, subject to further discussion, measures to help the Northern Ireland milk producers;

Or abandoning the present control system either forthwith or over a transitional period designed to avoid undue disruption to the doorstep delivery system and to prepare the way for the likelihood of imported milk.

14. If you decide on a more radical approach over a transitional period you will wish to invite the Agriculture Ministers to arrange for further work on the options by officials of their Departments and of the Treasury, the Foreign and Commonwealth Office, Trade and the CPRS. You will also wish to record whether implementation of the Binder Hamlyn proposals should be suspended pending further consideration of the options.

RtA

(Robert Armstrong)

18th March 1981

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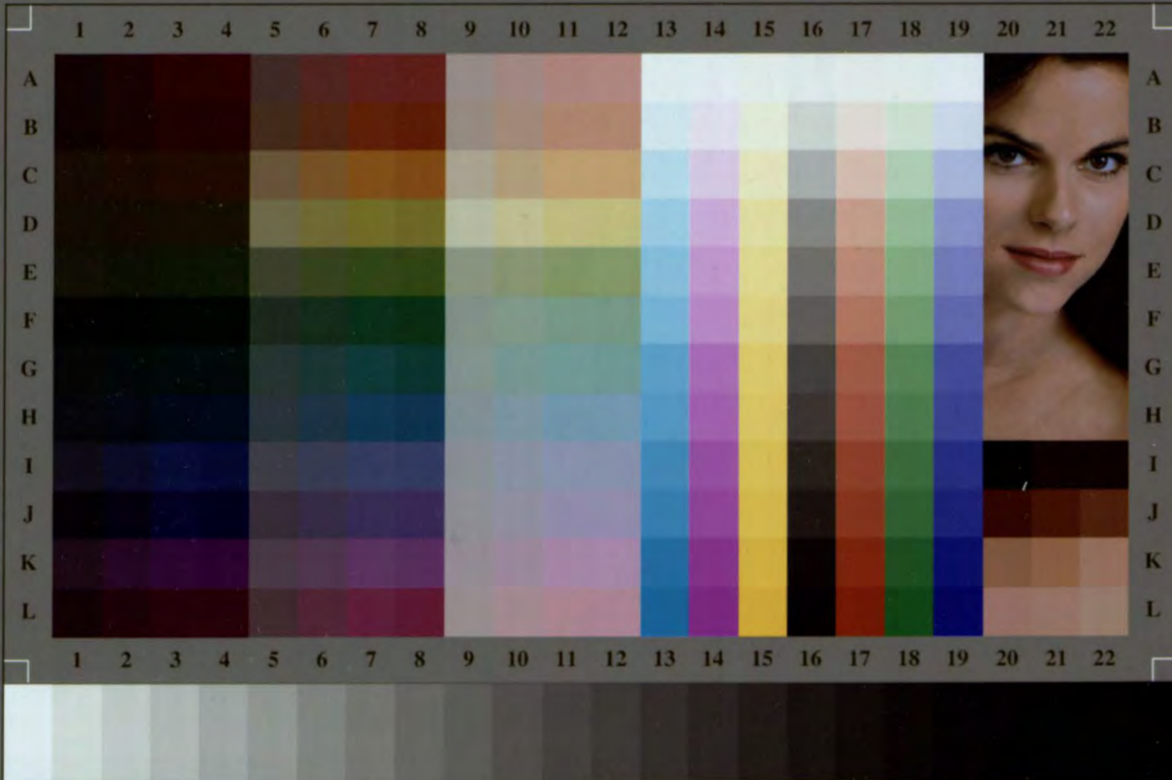

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