

COVERING CONFIDENTIAL



Foreign and Commonwealth Office

London SW1A 2AH

18 May 1979

*Dear Bryan,*

Call on the Prime Minister by the President of  
the European Commission

/ As requested in your letter of 11 May, I enclose a brief for the Prime Minister's discussion with Mr Jenkins on 21 May. It has been agreed with the Cabinet Office and takes account of comments from the Whitehall Departments concerned. It includes (paragraph 15) a description of the present state of play on the Commission's objection to the Interest Relief Grant Scheme for Offshore Supplies.

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

*Yours etc.*

*Paul*

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Private Secretary

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CALL ON THE PRIME MINISTER BY THE PRESIDENT OF THE  
EUROPEAN COMMISSION, 21 MAY

INTRODUCTION

A 1. Mr Jenkins will be primarily interested to hear the Prime Minister's personal approach to the Community. He will come briefed by Commission officials with counter-arguments to a number of the criticisms which the UK has made of the Community in the past. He has already made some comments in his speech to the Confederation of British Industry on 16 May (Text at Annex A). He has been very slow to appreciate the reality and importance of issues like the Community Budget. But he is now waking up to the fact that there is a serious problem and that something will have to be done about it this year. The Prime Minister will wish to stress the need for the Commission's full backing and in particular their readiness to come up with proposals for effective remedial action which could be adopted by the European Council before the end of this year.

B 2. In addition to setting out the Government's general approach to Europe (copy of speech at dinner for Chancellor Schmidt at Annex B), the Prime Minister may wish to be fairly specific about the Community problems she wishes to see tackled. These are covered below by means of Part I: suggested Speaking Notes; and Part II: supporting Background. Since Ministers are still looking at some of them the line to take is largely designed to elicit Mr Jenkins' views and comments.

PART I: SPEAKING NOTES

The Community Budget

C 3. We cannot easily sustain our pro-Community line at home when all the evidence suggests we are seriously disadvantaged by the working of the Community Budget. But before we can get remedial action taken, we need to get wider acceptance of the scale of our problem in 1980 and afterwards. We now have authoritative Commission figures for 1978 (table at Annex C), although Chancellor Schmidt still disputes them. Can we have a Commission estimate for 1980 when the transitional arrangements for the UK will have ended?

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4. I have heard about the argument on the attribution of MCAs and it is clear to me that the exporters benefit - they would not sell their produce to us without MCAs to subsidise it. It would make economic nonsense to attribute the MCAs as receipts to the UK when all they do is to offset part of the resource cost of buying expensive Community food. But in any event MCAs look like being very much reduced next year.

5. Similarly there is anyway a need to define more precisely the impact on the problem of some of the proposed solutions. For example, what do you think are the chances of meeting our needs through changes in existing policies, given:

- (a) the difficulty of getting the cost of the CAP down in any reasonable time scale;
- (b) the reluctance of the Germans and others to contemplate increasing expenditure of benefit to the UK on a scale which would deal with our problem;
- (c) their even greater reluctance to change the "own resources" system of financing the Budget?

6. We must get action this year. What do you think are the chances of getting the European Council in June to accept that remedial action must be taken to deal with our Budget problem, and to ask the Commission to come forward with proposals to this effect in time for them to be worked upon and approved at the European Council in November?

7. What proposals? Do you think that the Commission could then put forward proposals for a corrective instrument? Such an instrument, either in the form of a new version of the existing financial mechanism or a different instrument altogether, would stand a much greater chance of winning acceptance if the proposals for it came from the Commission rather than from the UK Government. Indeed I am advised that, if we are not to be accused of embarking on another "renegotiation", we must try to let any proposals for a solution emerge from the discussion rather than put them forward ourselves. Schmidt warned me of the danger of appearing to start another "renegotiation".

/Common

Common Agricultural Policy

8. The central problem of the CAP is the excessive expenditure which results from the disposal of surpluses, generated by support prices which are too high. We have seen estimates that the total cost of the CAP could reach £7,289 million (10,879 mEUA) by 1980. Is this right? What is the Commission's latest view about the rate at which expenditure will grow?

9. The first priority must be to put a stop to the growth in this expenditure and we strongly support the Commission proposals for a price freeze in 1979/80. It is essential that the Commission should stick to their proposal for a price freeze. There is no justification for any increase where there are structural surpluses.

10. The ultimate target should be prices set at a level where there is no incentive to produce more than is required for consumption, trade (without export subsidies) food aid and normal stocks.

11. But this will take time. We must get the cost of the CAP under control now. We cannot go on with the imbalance of Community expenditure on agriculture. It is clear that Schmidt is not going to be willing to increase own resources to pay for it. Some way must be found of containing and then reducing the cost. This is pre-eminently the role of the Commission to propose.

Common Fisheries Policy12. (a) Government Policy on CFP

The Government is determined to secure improvements to the existing Common Fisheries Policy. As I explained to Chancellor Schmidt on Thursday 10 May, this is a matter to which the Government and the country attach great importance. Whilst, therefore, we hope that discussions with our Community partners can now be undertaken in a better spirit, there should be no illusions that the Government will not seek vigorously to meet legitimate UK interests.

(b) UK National conservation measures

The Government considers it of the highest importance to protect fish stocks for the future. We would prefer this to be achieved by collective action, but until agreement can be reached on a Community basis we are obliged to proceed with some national measures, though for practical reasons we shall not be introducing until 1 July those which the previous Administration announced for 1 June.

What  
practical  
reasons?

(c) Handling of CFP negotiations

It is important that sufficient time is allowed to undertake adequate preparation for the next substantive discussion of fisheries.

The issues are complex and politically very sensitive in the UK. HMG wants to play a constructive part in the search for a satisfactory settlement. But they need time to prepare the ground, at home, and in bilateral contacts with the Commission and other EEC partners. Premature discussion could be counter-productive. Given preoccupation with the agricultural prices it seems impossible to prepare properly for a Fisheries Council to be held before July.

European Monetary System

13. I am aware that EMS has been suggested as a touch-stone for our attitude to the Community. You spoke about it yourself in your speech on 17 May here in London. The Government have welcomed the development of the EMS and we shall consider afresh the participation of the UK in its various aspects. But you will realise we have to consider all the implications of joining the exchange rate regime for the Government's economic policies, which we must first get right. We shall look at the matter again when the divergence indicator mechanism is being reviewed in September.

Energy

14. I am aware that the Paris Summit and the March Energy Council decided that Community Energy Policy should in future be regarded as the sum of the national energy policies of the member States, supplemented where there is a need by measures at the Community level.

? } I understand that you told the Foreign Secretary that the UK had a major role to play in the development of Community energy policy? What in particular do you have in mind? How would it relate to the Paris Summit criteria? We will be prepared to play our full part wherever there is a sound and acceptable case for Community action; we will expect others to do the same on matters of interest to us, such as coal. We believe the particular need is for Community external solidarity in the energy field when facing up to the dangers represented by the present oil market situation.

15. So far as our North Sea policies are concerned these involve vital national interests and there are both legal and political problems; but it should be possible to overcome them if we approach them in the right way. I am sure you realise that to confront a

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new Government in its first hours, as Commissioner Vouel did over the Interest Relief Grant Scheme, is not the right way. We start from a very different approach to the Community and we shall need time to work out our policies.

#### Industrial Policy

16. (a) This Government's general approach to industrial policies will be different from that of the previous Government. We will move away from short term palliative measures of support for industry towards longer term schemes, including investment in infrastructure. We hope that the Commission will devise positive policies in these areas. We would expect this approach to be more in line with that of the Commission, particularly on state aids and competition policy.

(b) In the next few weeks, the Government will review policies in support of sectors in trouble, including shipbuilding. We hope the Commission will not press us during this period. A specific problem is the case of the Fishguard/Rosslare ferry. The order from British Rail went to Harland and Wolff. The Commission have refused to approve the order until HMG give an assurance that future orders which involve Government subsidy should be tendered among all Community yards. This seems unreasonable. We have no power to dictate to firms to tender in a particular way. [REDACTED]

Would you be prepared to take this up with Commissioner Vouel yourself? Or would you prefer us to do so?. You will understand that any loss of employment in Northern Ireland that can be blamed on the Commission would have the most serious political implications.

/PART II: BACKGROUND

## PART II: BACKGROUND

The Community Budget

17. Mr Jenkins may be unwilling to give estimates for 1980. Commissioner Ortoli dodges round the issue whenever he is asked to produce them. Mr Jenkins should therefore be given the strongest incentive to get them out.

18. The first official Commission figures on the size of contributions were published in the Economic Policy Committee Report of November 1978 in connection with the so-called "concurrent studies" exercise related to the European Monetary System. The figures published in the report were for the three years up to 1977. Updated figures covering 1978 were published by the Commission on C 6 April 1979 (Annex c).

D 19. The question of the attribution of Monetary Compensatory Amounts is set out in detail at Annex D.

20. The point of the questions in paragraph 5 of the Speaking Note is that the chances of meeting our needs through changes in existing policies are nil. Mr Jenkins must be brought to realise this. And to improve on the Commission's preparations for study by the European Council.

21. The European Council of March 1979 invited the Commission and Council to make an in-depth examination of the contribution of the Community instruments to the achievement of convergence. This report has been prepared by the Co-ordinating Group and has been examined in draft by the Finance Council. At present it does not reflect the importance we attach to the economic effect of the present adverse resource transfers. However it does represent a beginning of a recognition of the importance of this problem. The final version of the report will be presented to the June European Council.

Common Agricultural Policy

22. The estimated cost of the CAP in 1979 is £6650 million and the bulk of this will be spent on three commodities, milk, cereals and sugar, which account respectively for 37%, 19% and 10% of the total. The cost is growing rapidly. Preliminary figures for 1980 are available and have been discussed at working level in Brussels. The

/1980



1980 forecast is 10,879 mEUA (£7,289 million), 13.5% above the budget provision for 1979 (9,582 mEUS). If MCA expenditure is excluded in both years, the increase is even bigger, at 16.7%.

23. Chancellor Schmidt suggested using the VAT 1% ceiling as a lever to contain the cost of the CAP. This would not suit us, since it would mean letting the cost grow for 2 or 3 more years, and not reducing its 75% share of the budget. We need earlier action to contain and then reduce the cost.

#### Common Fisheries Policy

24. The French Presidency have announced their intention to hold a Fisheries Council in June. In view of the lack of preparation and the prospect of an agricultural price-fixing "marathon" in June it will be difficult for this Council to make progress on the substantive CFP issues. A relatively low-key Council/<sup>in July but not sooner</sup> could enable preparatory work to be undertaken by the Commission and member States to enable progress to be made at a subsequent Council.

25. Mr. Jenkins may ask about HMG's intentions on the national conservation measures which the previous Government had told the Community it intended to introduce on 1 June, if satisfactory Community measures had not been agreed before then. The Minister of Agriculture, Fisheries and Food will tell the House on Friday, 18 May that, for practical reasons, these measures will be implemented on 1 July. He has explained to Vice-President Gundelach why HMG feels that it cannot withdraw from the course of action announced to Parliament by the previous Government in March.

#### European Monetary System

26. Mr Jenkins is likely to be interested in the new Government's attitude to the European Monetary System. In his speech in London on 16 May he argued that this was another European bus which Britain ought not this time to miss. The Prime Minister is recommended not to be drawn into detailed discussion of this. If necessary she could say that she fully recognises the potential benefits of EMS for currency stability and for the evolution of the Community. She will consider the matter carefully in this light later on, taking into account also all the other aspects of domestic and external economic policy.

/27.

27. At her press conference with Chancellor Schmidt the Prime Minister said that we shall have considered our position by September and therefore will be prepared to take up a position when the System is reviewed. We are now considering separately whether to exercise our option to swap 20% of our gold and dollar reserves for ECUs.

Energy

28. The Commission had raised with the previous Government the compatibility with the Treaty of Rome of the Department of Energy's Interest Relief Grant Scheme for Offshore Supplies. After discussing possible modifications to the Scheme with the previous Government over a period of about 2 years, the Commission published, on the eve of the election, a Decision requiring the UK to abolish the Scheme within 2 months, failing which we are likely to be taken to the European Court. The future of the scheme will be discussed by Ministers in E Committee on 23 May and the reply to the Commission drafted in the light of their conclusions.

29. At the end of last year Commissioner Davignon set out the Commission's difficulties with certain UK North Sea policies, particularly:

- (a) the requirement for North Sea oil and gas to be landed in the UK unless we agree otherwise;
- (b) the Offshore Supplies Office policy requiring North Sea operators to give full and fair opportunity to British industry to compete for orders of goods and services for the UK Continental Shelf (UKCS); and
- (c) the requirement for licencees operating on the UKCS to have their "central management and control" in the UK.

He indicated his wish to find a compromise by which the Commission could accept these policies subject to satisfactory UK assurances on their application. These policies cover important UK interests; but a substantive UK response to M. Davignon's approach has to be determined and this may offer the new Government an opportunity to explore the possibility of reaching an understanding with the Commission on these issues without compromising the UK's basic interests.

/Industrial

Industrial Policy

29. British Rail have placed an order with Harland and Wolff for a new Fishguard/Rosslare ferry. The Commission have refused to approve this order until HMG give an assurance that future orders to Harland and Wolff which involve Government subsidy should first be tendered among other Community yards. This order, which is the fourth in a series, is of great importance to the shipyard, is small in value (£17.8 million), involves a relatively small subsidy (6%) and is urgently needed by British Rail by September 1980. The Northern Ireland Office are recommending that their Secretary of State should write to the Prime Minister asking that she raise this point with Mr Jenkins.

External Issues

30. It is possible that Mr Jenkins may allude briefly to current external issues. The most important are:

- (i) Enlargement, where the Greek Accession Treaty is to be signed in Athens on 28 May, and the negotiations with Portugal and Spain are likely to get going in earnest after the summer.
- (ii) The MTNs on which the Commission can be congratulated on their major contribution to the successful outcome now emerging. The main outstanding points are accurate implementation of the results by the US Congress and completion of the negotiations on the question of safeguard action. Recognition of the possibility of selective safeguard action has been a major EEC objective.
- (iii) Japan. The problem of the Japanese surplus will be discussed at the European Council a week before the Tokyo Summit. The Community has been pressing Japan for several years and with only limited success, to take steps to reduce the surplus. The Japanese Foreign Minister will be in London on the same day as Mr Jenkins.
- (iv) Renegotiation of the Lomé Convention. The final Ministerial negotiating conference is due to take place in Brussels on 24/25 May. The main outstanding

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points are the size of the new European Development Fund, Human Rights, certain trade matters (notably the safeguard clause and rules of origin), industrial co-operation, and the question of assistance for mineral producing African, Caribbean and Pacific countries.

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