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THE BUDGET/CONVERGENCE: TACTICSBrief by H M Treasury

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1. The structure of the discussion of this item which we would like is:-

- a. Prime Minister's opening statement;
- b. agreement that we should get 520/630 meua by reform of the Financial Mechanism;
- c. discussion of, and agreement on, other possibilities to supplement b. so as to solve our problem.

2. An opening statement. It is likely that the Prime Minister will be expected to make an opening statement on the agenda item about the UK contribution to the Community Budget. The object of such a statement might be to direct discussion towards solutions; and to achieve as much acceptance as possible that changes which eliminate only one-third of our net contribution are nowhere near enough.

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3. For that purpose the statement might avoid going too far into the general arguments against us (North Sea oil, juste retour, trade orientation etc). It might instead reiterate the desire of the UK Government to put our relationship with the Community onto a sound, durable footing, referring to what the Prime Minister said about this at Strasbourg. It might say that the present scale of our contribution was however an inequity which no British Government could accept and which no other Head of Government would accept in a comparable situation. The Community itself had recognised in 1970 and 1975 (preamble to Dublin Mechanism) that such a situation would be a threat to the Community itself. And the danger to the Community and to ourselves was made worse by the state of the UK economy. Opportunities to avoid or rectify this situation had been missed in 1970 and 1975. It must be put right now.

4. We were grateful to our partners for the degree of recognition of our problem they had already shown. Nevertheless one-third or one half solutions were not enough. A one-third refund would leave our contribution in the area of that of Germany and a multiple of that of France. This could not be right. It must be reasonable, in the situation of our economy, that we should at least pay no more than France, which had been in a position of broad balance over recent years.

5. The statement might then say that we welcomed the wide acceptance which seemed to exist of the need to reform the present Financial Mechanism so as to yield us between 520 and 630 meua, according to whether we contributed to our own refund. We hoped that could be speedily agreed. But it could be only a first step and a partial solution. It would be essential to look at other possibilities. Some of these could be specified.

6. The statement might conclude by proposing that discussion concentrate on solutions.



7. The 520/630 meua. The objective might then be to try to secure agreement as speedily as possible to removal of the restrictions etc from the Financial Mechanism so as to give us the maximum possible (520/630 meua). One way of doing this would be to instruct officials to submit proposals for amending the Mechanism so that, so long as we were below Community average GNP per head we could count on paying no more than our GNP share. That would enforce removal not only of the critical conditions:-

- i. balance of payments deficit;
- ii. tranche system;
- iii. 3% ceiling

but also the merely dangerous ones (eg GDP per head below 85% of average, growth rate less than 120% of average etc). Any less precise direction could expose us to wrangles about these restrictions.

If there is doubt, the Prime Minister may wish to read out a list of the restrictions she wants removed.

8. Argument may develop on whether all Community members are to finance the reformed Mechanism. That is what the present Mechanism provides. Our best tactic may be to leave it to the Italians and Irish to argue for exemption. If they succeed, we too ought to be exempted from paying for our refund, and should say so. The reformed Mechanism would then be worth £400m to us, not £350m. However we do not want dispute about this to delay agreement on the revision of the Mechanism. If necessary the question of who pays might be left open - but then the presumption would be against the Irish, Italians and ourselves.

9. Further contributions to solving our problem. The next objective will be more difficult to achieve: securing discussion of additional possibilities to help us beyond the reformed Mechanism. At this point the Prime Minister might refer to 3 possible areas which have been discussed in the Commission papers:-



- i. improved receipts for the UK;
- ii. a framework for future expenditure on lines proposed by Italy, intended to change the balance of budget spending;
- iii. application of weighting to the improved Financial Mechanism, so as to treat our GNP for that purpose as reduced by the fraction which our GNP per head bears to Community average GNP per head (producing roughly 12% instead of 16%).

10. Of these the first is far away the most promising. The second is minor and uncertain. The third has been widely opposed, though it could yield what we need. The Prime Minister could argue that they are all communautaire, reflecting the now established principle of special protection in the budget for members which are less strong economically.

11. The important point on receipts is that any action ought to be on a substantial scale to meet our problem. Taken action of the 100/200 meua variety would not be enough. We should argue that the UK can be distinguished because it is a net contributor, its receipts are way below Community average and so is its GNP per head. A country meeting all 3 conditions ought to have a special arrangement to bring its receipts up to Community average, or up to its GNP share (the latter is strictly more logical, because we affect the average). We would clearly prefer an unconditional mechanism, but need not rule out some link to existing UK public expenditure of a structural or investment character.

12. If discussion of receipts (which the latest Commission paper choses to call "expenditure") gets that far, the question who pays will probably arise again. Italy and Ireland would have an every stronger case for exemption. So then would we. But this might fortify the determination of others to stick to universal payment for the improved 1975 mechanism.



13. It is not possible to foresee now in any detail how a discussion on receipts (or eg on the Italian plan for guiding expenditure) might develop. If enough were offered on receipts to make up, with the reformed Mechanism, an acceptable solution, well and good. If however:-

- i. the reaction were totally negative, or
- ii. a small amount were offered under the receipts heading, or
- iii. there were a proposal for some further study or Committee,

then (in all these circumstances) the Prime Minister might wish to seek a further early meeting of the European Council. Any study under iii. would have to report to that.

H M TREASURY

23 November 1979