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PRIME MINISTER

COMMUNITY BUDGET MANDATE : THE NOVEMBER EUROPEAN COUNCIL

As you know, I unfortunately cannot be present at OD tomorrow. I am therefore sending you in this minute my views on the important matters which OD will be discussing.

State of Play

2. It seems clear that the starting point for most of our partners in the Community, and possibly the Commission too, will be to look for a solution to the UK budget problem which leaves us worse off than foreseen last year under the 30 May system: i.e. a UK net contribution of more than 730 million ecus. That, at any rate, is the signal which the French and others seem at present to be transmitting; and the French want the new solution, like the old, to be temporary.

3. The scheme which the Commission has placed on the table is compatible with a wide variety of outcomes. Indeed, the main point about the scheme is that its effects are unpredictable. The effects on the UK would depend crucially on what we could negotiate for the critical parameters - in particular, the rate of compensation under the FEOGA mechanism and the nature of the financial mechanism on the contributions side. To obtain a reasonably secure presumption of a net contribution which was on average either modest or zero we should need a combination of a very high compensation rate (100 per cent or very close to it) under the FEOGA mechanism; and an "ideal" financial mechanism which went well beyond the present one and gave us full and unconditional reimbursement of the difference between our Community GDP share and our uncorrected share of own resources.

/The effects

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The effects would also be likely to vary substantially from year to year (see the illustrative figures at the Annex, based on estimates for 1981 and 1982). Unless we are very successful in the negotiation, it would thus be difficult to establish publicly that a settlement based on the Commission's scheme was better than (or even as good as) the 30 May settlement.

4. We, for our part, have put forward publicly - both in my Hague speech and in the Community itself - an approach to the Community budget which we genuinely believe would be in the Community's best interests and would solve the German problem (and the budgetary problems of enlargement) as well as our own. We have also outlined to the Germans - but not at this stage put forward publicly - a less radical corrective scheme which (a) is closer to one strand in the German Government's own thinking, (b) is consistent with a zero or small net contribution, on a predictable basis, for the UK and (c) would not involve excessive changes in the positions of individual member states compared with the existing, post-30 May position. We await considered German reactions. There are probably differences of opinion in Bonn. Chancellor Schmidt seems still to want a limit for Germany (as do the German Finance Ministry). They could not in fact get this under the Commission's scheme. But some in the German Foreign Ministry would be willing to settle for the Commission's scheme and for a modest gesture from the Commission in the form of a reduction in the cost to Germany of relief to the UK under that scheme. And although Chancellor Schmidt is reported to have said privately that there was really no reason why the UK should be a net contributor, there is naturally much resistance in Bonn to a low or zero net contribution for the UK, especially from those who are ready to accept the minimalist solution for Germany.

Next Moves

5. Looking ahead, there are 5 points which I particularly want to make. The last 2 are closely in line with what Peter Carrington and Peter Walker have already suggested. The first 3 are other points to which I attach special importance.



6. First, we must continue to signal to our partners that there is no justification for a less prosperous country like the UK being a net contributor at all. We must counter the signals from other member states that they are looking for an outcome for the UK worse than that envisaged on 30 May 1980. If we dilute or weaken our own signal prematurely, we shall simply redefine the target area for the negotiations to our own disadvantage. All this is compatible with hinting to the Germans that we are reasonable people and do not necessarily rule out making some small contribution to the allocated budget as at present defined at the end of the day - in addition to the substantial contribution we anyway make to the unallocated budget. But we must not give the impression that we can be driven back to the 30 May level or beyond.

7. Second, I think it would be a mistake to fall back on the Commission scheme at this stage in the interests of promoting a more orderly negotiation. I hope that Peter Carrington is not suggesting this in paragraph 4 of his minute of 6 November. It would, I believe, be wrong to retreat abruptly from our existing position. To do so would convey the wrong signal about our requirements from the negotiation. Neither could we possibly rely on negotiating a version of the Commission scheme which represented a good deal for the UK - least of all if we agreed to the method now. As the annexed estimates illustrate, the only version of the scheme which might give us a reasonably secure presumption of getting rid of our net contribution, or reducing it to something small, would be one in which all the critical parameters were settled in a manner exceptionally favourable to the UK.

8. Third, I think we need to consider whether, subject to Chancellor Schmidt's reaction at the talks on 18 November, we ourselves should table the corrective scheme which we have shown to the Germans. Although Peter Carrington's minute does not discuss the point, there is in my view a considerable prima facie case for doing this. I believe it could be put forward without pinning our colours irrevocably

/to it,



to it, as an alternative which was more firmly based on principle than the Commission scheme and more likely to be a lasting solution for the Community. And it would be evidence of our efforts to make progress on the Budget during our Presidency: evidence which is lacking in public at present. It would make clear our requirements from the negotiation and remove the situation in which there is only one scheme - the Commission's - on the table. In doing so I believe it would increase our leverage in the negotiation.

9. A further consideration is that we must expect the substance of our exchanges with the Germans to reach others, especially the French and the Commission: this may already be happening! So our scheme is quite likely to become public anyway.

10. You will anyway wish to discuss our new scheme with Chancellor Schmidt and a final decision on making it public will have to take account of Schmidt's reactions. If however there should be any degree of support from Schmidt - even on the lines that the framework if not the figures provide one possible basis for the negotiation - then the case for outlining our new scheme publicly would be particularly strong. Even if Schmidt is non-committal, there would still, I suggest, be a case for outlining it publicly, along with the Hague speech approach, while referring at the same time to the Commission scheme as another possible route.

11. My fourth point is concerned with the question, already discussed in the papers by Peter Carrington and Peter Walker, of the possible need at some stage for concessions on the agricultural chapter. I am sure that Peter Carrington and Peter Walker are right when they suggest that a link is likely to develop between the French demands on the CAP and our own demands for satisfactory budget refunds. I entirely agree with Peter Walker that we should withhold any specific concessions to the French until we have an equally specific settlement on the budget refund. I also agree in general with his conclusions as to the points on which we might in due course offer the French some limited concessions (export /contracts and



contracts and cereal substitutes) and those on which we cannot (vegetable oils and oil seeds). I am concerned at the signs that the French may continue to demand that small producers in the milk sector should get some special treatment, as their price for a satisfactory budget settlement. We should clearly resist this at present. But I believe we should now start to consider whether there are any ways in which some concession to the French might be made at a tolerable cost to our budgetary and agricultural interests: for example, by offering some degree of exemption from the basic co-responsibility levy to small producers, provided this was clearly identified as an income aid and nationally financed.

12. Also on agriculture, the likely linkage between the budget refund negotiations and next year's price fixing requires in my view that we must continue to press for the European Council guidelines on CAP prices and the rate of growth of expenditure to be as toughly worded as possible. Our aim should therefore be to stick as closely as we can to the text - the full version of alternative A on prices and alternative D on the rate of growth of expenditure in the draft guidelines of 6 November - which we have hitherto been supporting in the Mandate Group discussions.

13. Finally, there is the question of what we should seek to obtain from the November European Council. I agree with Peter Carrington that an all or nothing approach would be wrong and that a 'half-success' could suit us pretty well. I suggest that our aim at the November Council should be:

- (i) to avoid discussing possible solutions in too much detail;
- (ii) to extol the virtues of a 'Community approach' to the budget problem and to avoid outright rejection of our scheme (assuming that we have tabled it); and
- (iii) to secure agreement on a set of guidelines for reform of the budget which would be compatible with either the Commission approach or our own. I believe that

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officials have already prepared draft guidelines on this basis.

Conclusions

14. To sum up, I hope that OD will be able to agree on:

- (i) the importance of continuing to send suitably robust signals to the Germans and other member states about our requirements from the negotiation;
- (ii) the importance of not abandoning our own approach or indicating willingness to negotiate on the Commission scheme alone;
- (iii) a provisional conclusion, subject to German reactions at the 18 November talks, in favour of tabling our new corrective scheme publicly - ahead of the European Council if possible;
- (iv) the need to avoid making concessions to the French or others on the CAP until we are in a position to trade any such concessions against concessions by others on the budget settlement; and
- (v) the aim of getting agreement at the November Council to guidelines for budgetary reform compatible with either the Commission or our own approaches.

15. I am copying this minute to other members of OD and Sir Robert Armstrong.

Peter Jenkins
for (G.H.)

11 November 1981

(Approved by the Chancellor of the Exchequer and signed in his absence).