Europe Pt

CONFIDENTIAL

Qz 02391

PRIME MINISTER

30 May Mandate: Follow up to the European Council

PURPOSE OF DISCUSSION

1. The meeting has been arranged in order to consider how the discussion of the 30 May Mandate at the European Council should be followed up.

HANDLING

2. It may be convenient to focus discussion on the issues set out in my minute of 1 December to Mr Alexander. But you may first ask the Foreign Secretary to explain what arrangements he has in mind for the meeting - probably at Lancaster House on 21/22 December.

Flag B

(i) Purpose of Foreign Ministers' Meeting

3. The Foreign Secretary will probably argue that it is not realistic to expect to get a detailed settlement on the budget in the next few weeks but that guidelines would be a worthwhile step towards full agreement in Spring 1982. The Chancellor of the Exchequer may also consider that the right budget guidelines would be worth having. The Minister of Agriculture on the other hand may argue that it would be better to prevent any agreement at this stage and hold out for a detailed package in the Spring. It is not reasonable to suppose that we can get agreement on figures for the budget if we are only arguing about guidelines for the CAP. The crux of the matter is that we should not enter into agricultural commitments which are more detailed and binding than the commitments we will seek to secure on the budget.

(ii) Minimum requirements on the budget

4. The three texts which were on the table at the European Council (UK Presidency, Commission, and French) are attached at 'A'. You will want to ask the Chancellor whether he considers the minimum requirements set out in paragraph 2(ii) of my minute to Mr Alexander are sufficient. The Foreign Secretary may question whether requirement (b) - a generally applicable corrective - is of crucial importance to us (as distinct from the Germans).

CONFIDENTIAL

/The Chancellor

The Chancellor will probably attach importance to the inclusion of "relative prosperity" - point (c) - on the grounds that it combats the principle of degressivity. The point could also be met by insisting that eg "the size of the corrective must be large enough to prevent the recurrence of unacceptable situations in any year"? On duration, it is unlikely that we could achieve an unlimited period and so the terms of any review will be crucial. It might be better to leave open the length of the period until later when it could be negotiated together with amounts. Others will see a connection between duration and degressivity.

(iii) Agricultural Issues

5. On the Mediterranean our concern is the risk of substantially increased expenditure rather than any wish to be unhelpful to Italy and Greece. Your suggestion of "examine with a view to improving" might provide the basis for a compromise. Our concern with the expenditure ceiling is also primarily budgetary. The present texts on the expenditure ceiling are attached at 'B'. We should aim for a compromise between alternatives 'A' and 'B'.

6. On both issues, the Chancellor may suggest that we maintain a common stance with the Germans and hold out so long as they do. In the last resort, our safeguard lies in an adequate budgetary corrective.

7. The major difficulty will be dealing with milk. We together with the Dutch and to some extent the Germans and the Italians do want effective action ("modulation of guarantees ") to penalise overproduction. This could take the form either of a supplementary levy or a reduction in the intervention price. We shall probably have to accept the continuation of the linear co-responsibility levy. But, as the figures at annex 'C' show an exemption from levy on the first x kgs, while it would save our producers some money, would save other countries far more. You will wish to know whether the Minister of Agriculture feels that there is any concession which could be made to what is clearly a major political requirement for President Mitterrand. One suggestion was included in Sir R Armstrong's minute of 20 November to Mr Alexander (see extract at 'D'). The phrase at the end "subject to suitable conditions" covers that possibility

FLAG A

/that member

that member states would be authorised to pay themselves part of the co-responsibility levy which falls on small milk producers whose principal income derives from milk.

(iv) Attendance at the Special Foreign Ministers' Meeting

8. If the Foreign Secretary is not in favour of Agriculture Ministers being invited a remark made by President Mitterrand at his Press Conference suggests that he is not either. You will want to know Mr Walker's views. As there are to be two officials, one of them should be from MAFF.

(v) UK Budget Limits Scheme

FLAG C — 9. In his minute of 24 November the Chancellor suggested that the Treasury's latest budget limits scheme should be made available to other member states. The Foreign Secretary may argue that to do so before the Foreign Ministers' meeting is likely to confuse the handling of the meeting. The Chancellor may be content provided there is agreement that it should go round in the New Year. At the right time officials should meet to consider the text.

CONCLUSIONS

10. You may be able to sum up

- that we should call a meeting of Foreign Ministers before Christmas although the prospects for a successful outcome are poor;

- that we should not settle for a budget text which does not meet the Chancellor's minimum requirements;

- that we should stick with the Germans over Mediterranean agriculture and the share of agriculture in the budget, and not concede on small milk producers beyond what the Minister of Agriculture believes is politically acceptable;

- that our aim should be to keep attendance to Foreign Ministers assisted by agriculture experts;

/ - that

- that consideration should be given to the Treasury's budget scheme after the Foreign Ministers' meeting.

M D M FRANKLIN

1 December 1981

CHAPTER III. BUDGETARY PROBLEMS

ANNEX A

A. TEXT PROPOSED BY THE PRESIDENCY

1. The object of the Community budget is to finance agreed Community policies. At the same time the creation or recurrence of an unacceptable situation for any Member State must be avoided and the overall convergence of the economies of Member States must be fostered, without imposing an undue burden on any Member State.

2. In the long term the reconciliation of these objectives will be achieved through the development of Community policies and of the balance between them. The conclusions reached in Chapters I and II above are a first step in that direction.

3. But the process of reconciling the objectives by these means will take a period whose length cannot be predicted with any precision and, in the meantime, a budgetary corrective arrangement will be needed, if unacceptable budgetary situations are to be avoided.

4. The corrective arrangement will need to deal not only with the problem already recognised by the Community when the financial mechanism was agreed, but also with the imbalance in the distribution of expenditure, notably FEOGA guarantee expenditure. The arrangement will be based on objective criteria, so that there will be no need for an annual negotiation. It will take account of relative prosperity as between Member States and progress in achieving balance in Community policies. It will also take account of the volume of net contributions of Member States with undue burdens which must be limited.

5. The financing of the corrective arrangement will be achieved within the agreed VAT ceiling, if necessary by a method which avoids any net budgetary impact: and without putting at risk the financing of other agreed Community policies. The financial effects of the corrective arrangement will have regard to whether the payments come from Member States below or above the Community average GDP per head and whether they already have a problem arising from the Community budget.

6. The corrective arrangement will apply with effect from the Community's 1982 budget year. The Council, acting on a proposal of the Commission, will take the necessary detailed decisions by 31 December 1981.

7. The detailed arrangements so agreed will be reviewed after seven years to consider the progress made towards the Community's long term budgetary objectives and whether any changes are needed.

.../...

B. TEXT PROPOSED BY THE COMMISSION

The European Council noted that all the work carried out since the submission of the Commission report complied with the Mandate of 30 May 1980 which aimed to resolve budgetary problems by developing or adapting Community policies without calling into question the principles on which they are based, particularly in the case of the CAP. The effects of the measures being prepared will not, however, be felt to any significant degree for some time.

For this reason, the European Council adopted the principle of financial compensation measures for the United Kingdom to be implemented as from the 1982 financial year. Such measures would be decided upon for a specific period. They should not affect the Community's financing system.

The amount of the compensation would be arrived at annually on the basis of the actual figures for each year using an objective indicator to measure the true extent of the problem and in the light of the agreed rates of compensation. In this way recurrent annual negotiation would be avoided.

The costs arising from the compensation paid to the United Kingdom would be shared according to an ad hoc scale to be decided upon by the Council in accordance with the policy of solidarity which the Community intends to continue to apply towards its less prosperous members and taking into account the specific nature of the German budgetary problem.

C. TEXT PROPOSED BY THE FRENCH DELEGATION

1. The European Council reviewed the Community's budgetary situation on the basis of the report from the Commission.

2. The European Council reçognized that a better balance between Community policies was necessary in order to create a sound basis for the further development of the Community.

3. The European Council noted that its conclusions concerning the develpment of Community policies and the adaptation of the common agricultural policy constitued significant first steps in this direction.

4. The European Council agreed that a temporary, exceptional common action, allowing for an alleviation of the budgetary burden of the UK, should be established, under which funds would be made available to the UK from the budget of the Community for a short period.

5. The European Council invited the Council (General Affairs) to fix, at its next session, the duration and the degressive, arbitrary amounts to be made available.

ALTERNATIVE A

17. It will be the responsibility of the Council, acting on proposals by the Commission, to adopt the necessary decisions on implementation of the above guidelines to ensure that for the time being agricultural expenditure will grow less rapidly than the Community's own resources. It will be the responsibility of the Commission to manage agricultural expenditure within that framework. [1]

ALTERNATIVE B (Proposal by the Danish delegation)

17. It will be the responsibility of the Council, acting on proposals by the Commission, to adopt the necessary so decisions on implementation of the above guidelines [which would imply] that for the time being agricultural expenditure will grow less rapidly than the Community's own resources. It will be the responsibility of the Commission to manage agricultural expenditure efficiently.

ALTERNATIVE C (Proposal by the French delegation)

17. The European Council considered that implementation of these guidelines by the Council should ensure that agricultural expenditure grows less rapidly than the Community's own resources, as has been the case over the last two years.

---

(1) The Commission suggests the following declaration:

"In the opinion of the Commission the implementation of the orientation adopted in paragraph 17 should be evaluated as an average over several years in the case of erratic evolution in the conditions under which the common agricultural policy is executed".

The Greek delegation has a reservation linked to Mediterranean agriculture

The Irish delegation has a reservation linked to the income situation in the farming sector

The Italian delegation has a reservation linked to the feasibility of the guideline in the event of falling world market prices.

.../...

ANNEX C

MILK CO-RESPONSIBILITY LEVY EXEMPTIONS

1. The Prime Minister asked for some details of the effects of exempting from co-responsibility the first 30,000 Kg of milk (approx 7-8 cows) and the first 120,000 Kg (30 cows) on each holding.

2. If the first 30,000 Kg are exempt, then 90% of UK milk pays the levy, compared with 51% in Germany, 63% in France and 48% in Italy. The UK would pay 22% of the total levy revenue (compared with 16% of the present co-responsibility levy). France would pay 24% and Germany 18%.

3. If the first 30,000 Kg of milk on each holding are exempt from levy, then at present prices and the present rate of levy (2.5%), UK milk producers would pay £52.5m, instead of £58.3m, a saving of £5.8m. The saving to German producers would be £41.7m, and to French producers £33.9m.

4. The saving to the individual producer who produces more than 30,000 Kg would be approximately £116 pa at present prices.

5. If the first 120,000 Kg is exempt, then 61% of UK milk pays the levy, compared with 7% of German milk, 6% of French milk and 10% of Italian milk. The UK would pay 43% of the total revenue collected, compared with 11% for France, 8% for Germany and 6% for Italy.

ANNEX D

Milk

Modulation of the guarantee should be achieved by a combination of:-

(a) a linear co-responsibility levy with the existing exemptions

(b) a supplementary levy on additional deliveries to dairies or modulation of the intervention price if production exceeds a guarantee threshold

(c) a possible limited exemption from the co-responsibility levy for a certain quantity of milk from each herd if warranted by price decisions and subject to suitable conditions.