SRWAOJ

DISCUSSION BETWEEN HEADS OF GOVERNMENT BEFORE DINNER DURING EUROPEAN COUNCIL ON 5 DECEMBER 1986

Heads of Government had a brief discussion before dinner on 5 December of the future financing of the Community.

The Prime Minister suggested that M.Delors should give an indication of how the Commission's review of the Community's finances was progressing. This was of course intimately bound up with the future of the CAP. The Community would soon confront a very serious financial situation which it could not run away from. No decisions were required at this Council. But Heads of Government needed to know the dimensions of the problem.

M.Delors said that the Commission would present three reports on financial problems, agricultural problems and cohesion. These reports were required by the conclusions of the Fontainebleau European Council and by the Single European Act. These tasks could not be fulfilled without taking stock of the CAP. By way of introduction he wanted to put three simple propositions. First, the Community would not get through 1987 without a major financial crisis. Second, reform of the CAP had now become inevitable. Third, the Community had to choose between two concepts of cohesion: either one based on compensation through the budgetary mechanism; or an economic area based on convergence of economic policies. The Commission favoured the second.

Financial problems

M.Delors continued that the Community budget had been in deficit for years and had only been saved from disaster by a series of expedients. These were to let agricultural stocks build up; to let a gap develop between commitments and payments; and to carry over a deficit from one year to the next. But it was no longer possible to get by by using these devices. The Community's budget for next year provided for

39 billion ecu: a more realistic figure would be 43 billion ecu. The Community might get through until July but thereafter would have to impose savage cuts, particularly in agricultural payments and the structural funds. He had therefore decided to ring the alarm bell. Member states should face up to decisions in the course of next year. The Community needed a stable and guaranteed financial system under which the Commission did not need to keep coming back for topping up. The Commission needed to know exactly what it could expect by way of resources between now and 1992. The choice was between:

(i) increasing the VAT rate from 1.4 per cent to 1.6 per cent. But that was not really an option because a realistic budget for 1987 would already require a rate of 1.65 per cent; or

(ii) to set a precise ceiling for the Community's revenue expressed as a proportion of GDP which would on no account be breached up to 1992.

CAP

M.Delors said that the crisis in the CAP was due both to internal causes and international factors. Even if one carried out the most far-reaching reform, it would not actually decrease agricultural spending, simply stop it from rising so fast. Production was increasing all over the world and there was little prospect of the Community finding new markets. Indeed it had done better than most people realised, for instance by increasing its share of the world market for cereals from 14 to 17 per cent. Going further down this course risked a trade war with the United States. He would therefore set out a number of measures which were, in the Commission's view, essential:

(i) steps must be taken to eliminate surplus stocks. The intervention system must return to the original concept of smoothing out market fluctuations. At present the technical and financial costs of storing surpluses were three times what the Community spent on research and technology;

(ii) a more realistic pricing policy was needed;

(iii) farm incomes must be protected. The Commission were divided on how best to secure this. He personally favoured income support, although many farmers' organisations did not like this.

(iv) The Community must pursue a vigorous external agricultural policy.

Everything else was merely technical. The basic question here was whether one preferred quotas or co-responsibility levies. Personally he believed that quotas worked best.

Cohesion

M.Delors said that cohesion was part budgetary and part an economic problem. The choices for dealing with it were either through a compensation mechanism which related contributions to GDP, or by creating a single economic area. The Commission was firmly attached to the latter, but to achieve it there would need to be a doubling of the structural funds between 1987 and 1992. M.Delors identified a number of hallmarks for cohesion:

(i) dissemination of prosperity through the internal market and technological cooperation;

(ii) stimulation of small and medium sized businesses;

(iii) use of the mechanisms of the CAP;

(iv) Community action in favour of less-favoured regions. Here support for programmes rather than projects was essential;

(v) reform of the social fund to enable it to concentrate on three or four major problems;

(vi) the Commission would propose setting up an environment fund.

Method

M.Delors said that he would be at the disposal of all heads of government in the early part of 1987 to visit them in their capitals, to explain the problems and to discuss with them the possible solutions.

The Prime Minister said that M.Delors' report had come as something of a shock. In plain terms, the Community was broke. Heads of government should have been told this before. They might have created an effective financial discipline. When you were broke there was no point in taking on increased expenditure. The most costly policies would have to be reduced. She agreed that it would be useful if M.Delors was to make his tour of Community capitals. The Commission should then set out options for the future with clear costings and the consequences spelled out. What had happened should not happen again.

Mr. Papandreou said that M.Delors had made a most important and significant statement. Clearly he wanted a united Europe. One would not get that by reducing spending. He agreed that it would be useful for M.Delors to visit capitals.

Chancellor Kohl said that M.Delors' report was shocking but not new. There was no point in belly-aching. Heads of government had to see how they could take matters forward. He agreed that it would be useful for M.Delors to make visits to capitals in January and February. After that the Commission should try and reach some conclusions and put forward options. On this he agreed with the Prime Minister. It would be necessary to devote a great deal of time to this problem. We were setting the points for the future.

<u>The Prime Minister</u> said that it was agreed that M.Delors should make his tour and then set out options with costs spelled out. There was in addition an immediate problem. The Agriculture Council was meeting next week. Heads of Government should instruct their Agriculture Ministers to take decisions on the milk and beef regimes. She had received a letter from the President of the European Parliament stressing the need to take decisions on agricultural spending. She repeated that it was now for M.Delors to make his tour of capitals and report further.

(C. D. POWELL)
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