3.14 CONFIDENTIAL

Prime Minister

Agree that this paper should be tabled in the first week of August?

A.J.C. 22/7.

CC Sir AP

Yes - but don't like supplementary budgets for CAP. MT

CHANCELLOR OF THE EXCHEQUER HONI SOIT QUI MAL Y PENSE

Treasury Chambers, Parliament Street, SWIP 3AG
01-233 3000

PRIME MINISTER

POST-STUTTGART NEGOTIATIONS:
A "STRICT FINANCIAL GUIDELINE" FOR AGRICULTURE

In my minute of 6 July about the "safety net" I mentioned that officials were also preparing a second paper, which might also be tabled in the negotiations following up the Stuttgart Declaration, dealing with a strict financial guideline for controlling agricultural expenditure. I enclose a text, (agreed between officials).

2. The paper starts from the principle, long advanced by us and the Germans, that "the rate of growth in agricultural spending should be markedly lower than that of the own resources base"; and it sets out how to build this into the annual budgetary procedures, so as to prescribe the amount available for CAP support each year. It deliberately avoids such terms as "ceilings" or "maximum rates". But the intention of our proposal - as our partners will readily see - is to give the strict financial guideline mandatory force, and so impose an effective financial limit on the decisions taken by the Agriculture Council, and on the subsequent management of the agricultural budget by the Commission.

3. There are a number of points in the paper to which I should draw particular attention. First, paragraphs 3 and 5 propose that the Community should formally specify in its budgetary procedures that the rate of growth of FEOGA guarantee expenditure should not exceed a "given fraction" of the rate of growth of the own resources base. Although the text does not say so in terms, the reference to "budgetary procedures" is intended to enable us to argue that the strict financial guideline should be written into the budgetary section of the Treaty. We shall need to make it clear that this is indeed what we have in mind. All agricultural decisions must be subjected to an external financial discipline, which the Agriculture Council itself cannot alter. Without such a discipline there will be no compulsion on the Agriculture Council to adopt policies of price restraint and tough guarantee thresholds.

4. Second, paragraph 13 provides that, in the last resort, supplementary budgets may be introduced, permitting agricultural expenditure to exceed the strict financial guideline in a particular year. This degree of flexibility in the operation is inevitable, to allow for fluctuations in world prices. But to ensure that the procedure is not abused, the proposal lays down a requirement of unanimity in the Council for the approval of a supplementary budget. In addition, paragraph 14 requires that any overspending through a supplementary budget in one year should be deducted from the amount available under the guideline in the following year. Without this penalty provision agricultural expenditure could continue to grow cumulatively faster over a period of years than the guideline demands. Equally, however, to preserve symmetry, paragraph 15 would allow underspending in one year to be carried forward so that expenditure is not permanently depressed below the target trend level.

5. There are two further points, not at present spelt out in the paper, on which we shall have to be ready to put forward more precise proposals in Brussels. First, we will need to put a figure to the "given fraction" of the own resources growth rate by which agricultural expenditure is to be allowed to grow. We need to set a tough opening target: I suggest that our opening bid should be two-thirds, and that we should aim to go no higher than three-quarters. We need not settle that immediately but ought to do so by the end of the month.

The Treasury will discuss this further with departments AR 22/7.

6. Second, paragraph 17 notes that one of the questions for examination in the negotiations is whether the Commission has adequate power to enable them to observe the guideline during the year. The difficulty here is that the various measures to adapt CAP regimes described in paragraphs 18-20 of the paper, while highly desirable, are directed at reducing the trend of agricultural spending in the medium-term, and might be insufficient to cope with short-term excesses in expenditure during the year. We must therefore be ready to put forward fresh ideas, eg. to allow the Commission to operate intervention in the year more flexibly, to respond to changes in world prices and to implement guarantee threshold penalties in the year in which the thresholds are exceeded. A number of such ideas are now being discussed interdepartmentally: agreement will have to be reached, if necessary in OD(E), by the end of the month.

7. Finally, I should emphasise that I do not underestimate the substantial opposition we are likely to encounter in putting forward our proposals. This paper will be even more unwelcome to our partners then our safety net proposal; and we shall be accused of seeking to undermine the CAP. On some of the detail we can be flexible. But the fact is that only a mandatory guideline will meet the need for an effective control of the rate of increase of agricultural expenditure; and without such control it would be very rash to consider increasing the Community's own resources.

8. We shall circulate our "safety-net" paper later this week. There are, however, good tactical reasons for holding back this second paper until the Commission has put forward its own CAP proposals: I envisage circulation in the first week of August.

9. I should be grateful to know whether you are content with the paper, and my proposals for its tabling.

10. Copies of this minute go to the Foreign Secretary, Members of OD(E), the Secretaries of State for Scotland, Northern Ireland and Wales, and Sir Robert Armstrong.

NL

(N.L.)

19 July 1983

A STRICT FINANCIAL GUIDELINE FOR CAP EXPENDITURE: BUDGETARY ASPECTS

A. Introduction

The Stuttgart European Council decided that the negotiations to take place under the special emergency procedure should cover the need for greater budgetary discipline. In particular, in relation to agriculture, the European Council declared that "the basic principles of the Common Agricultural Policy will be observed in keeping with the objectives set forth in Article 39 of the Treaty establishing the EEC and that the Common Agricultural Policy must be adapted to the situation facing the Community in the foreseeable future in order that it can fulfil its aim in a more coherent manner." The list of questions to be examined in the present negotiation includes the need for strict financial guidelines and the European Council further declared that:

> "The examination will result in concrete steps compatible with market conditions being taken to ensure effective control of agricultural expenditure ...".

The present note outlines accordingly the United Kingdom's suggestions for the introduction of a strict financial guideline. The United Kingdom will also in the course of the negotiations participate fully in the discussion of the other agricultural issues listed in the declaration of the European Council with a view to a satisfactory result on the agricultural chapter as a whole.

2. The European Parliament, in the Arndt Resolution, said that the annual increase in agricultural expenditure must be held at a lower level than the increase in revenue. The United Kingdom has consistently taken the position that the rate of growth of agricultural expenditure should be markedly lower than that of the own resources base; and has proposed that this guideline should be observed by the Council of Ministers (Agriculture) in its decisions in the annual price fixing, by the Council of Ministers (Budget) in establishing the Community's budget and by the Commission in its management of the funds provided in the budget for agricultural expenditure.

3. It is the view of the United Kingdom Government that, in order to ensure the effective

control of agricultural expenditure and to achieve a better balance in the Community budget between agriculture and other policies, this guideline should now be adopted by the Community and formally embodied in an effective way in the Community's revised budgetary procedures.

B Proposed budgetary procedures

4. The United Kingdom Government suggests that this guideline could be embodied in a financial framework forming part of the Community's budtary procedures in the following way.

5. The strict financial guideline to be adopted by the Community shall specify that the rate of increase in FEOGA guarantee expenditure in any year, when compared with the corresponding provision in the original budget adopted by the European Parliament for the preceding year, shall not exceed a "given fraction" of the rate of increase of the own resources base between the two years. (The present negotiations will need to fix the size of the "given fraction").

6. Simultaneously with its annual price fixing proposals the Commission shall make a reasoned proposal for the actual rate of increase in the amount available for FEOGA guarantee expenditure in the budget for the year following the price fixing, compared with the amount provided in the original budget for the year of the price fixing. The Commission's proposal may be for an increase lower than the rate specified by the "given fraction" but shall not exceed it; The Commission's price fixing proposals will need to be consistent with the proposed rate.

7. As early as possible in the year the Council of Budget Ministers shall examine the Commission's proposed rate of increase (including the forecast increase in own resources) and vote on it. The Commission's proposal shall be adopted unless the Council decide by a qualified majority to amend it. The Council may not, however, vote for a figure in excess of the maximum rate specified by the "given fraction".

8. The Council of Ministers (Agriculture) shall ensure that their decisions in the price fixing and at other times are consistent with the observance of the guideline rate of increase as adopted under the procedure in paragraph 7. If, however, in the course of the price fixing negotiations, the Commission wishes to propose an increase in the guideline within the total set by the "given fraction" a joint Budget/Agriculture Council would be called to reach a decision on the rate of increase to apply to agricultural spending. The Joint Council may not decide on an increase in excess

of that specified by the "given fraction

9. As the European Parliament has recommended on several occasions, the revenue from coresponsibility and other levies imposed in the agriculture sector should not be classified as negative expenditure or used in any other way to increase the amounts available for agricultural expenditure.

10. The Commission's proposal for FEOGA Guarantee expenditure in the Preliminary Draft Budget for the year following the price fixing shall conform to the Council's decision on the strict financial guideline as taken under paragraphs 7 and 8 above. The Council shall likewise conform to the guideline in establishing the draft Budget. It shall be open to the Parliament, in the course of the budgetary procedure, to propose modifications which would increase agricultural expenditure beyond the rate of increase specified by the "given fraction" laid down in the guideline in paragraph 5 above, provided it has first voted for such an increase in that maximum rate acting by a majority of its members and by 3/5ths of the votes cast. The Council may accept such modification, provided that it has also agreed, voting by qualified majority, to adopt the new financial guideline proposed by the Parliament.

11. The Commission shall aim to manage agricultural expenditure during the year within the amount laid down in the adopted budget.

12. If during the course of the year it appears to the Commission that the amount available for agricultural expenditure is in risk of exhaustion, the Commission shall make proposals to the Council for reducing the growth of agricultural spending.

13. If, however, because of unforseeable circumstances, it appears to the Commission that, even after resort to exceptional measures, an increase in expenditure from the FEOGA guarantee section is unavoidable, it may, after 1 October, present a supplementary budget for this purpose. If necessary, this may be accompanied by a proposal for a higher rate of increase in FEOGA Guarantee expenditure in that year than that specified by the "given fraction". Where the Commission's proposals require such an increase the Budget Council will vote on the proposed new guideline, acting by unanimity. Subject to this vote, the Council shall act on the Commission's proposals for increased expenditure by qualified majority. The Parliament shall vote on the proposed new guideline by a majority of its members and by 3/5ths of the votes cast.

14. When agricultural expenditure in any year has exceeded the amount specified by the "given fraction" either on a proposal from the Parliament (see paragraph 10 above) or by

the adoption of a supplementary budget (see paragraph 13 above), the amount of the excess shall be deducted from the amount available under the "given fraction" rule in the following year. To this end the Commission should propose the necessary compensatory reduction in the following year's budget by means of a rectifying letter. When such a deduction has been made, it shall be ignored for the purpose of calculating the financial guideline for subsequent years.

15. Where the total of FEOGA Guarantee expenditure in the year has for any reason (including compensatory reductions made in accordance with paragraph 14) fallen below the maximum permitted by calculation of the given fraction, the amount of any such shortfall may, on the proposal of the Commission, be added to the amount available under the given fraction for the following year, provided the Council of Budget Ministers shall decide to adopt the proposal, voting by qualified majority. When such an addition has been made, it shall be ignored for the purpose of calculating the financial guideline for subsequent years.

C Implementation of Financial Framework

16. The adoption of this financial framework will not in itself be sufficient to guarantee that it is observed. It will need to be accompanied by detailed decisions to ensure that expenditure is kept within the guidelines. These decisions will be taken by the Council of Agriculture Ministers and, to the extent appropriate, by the Commission.

17. In the first place the annual price fixing will need to be conducted within the overall financial limit previously set by the Council of Budget Ministers for guarantee expenditure in the following year's budget. Secondly, should the trend of expenditure in the course of the year exceed that expected by the Council at the annual price fixing and incorporated in the budget provision for the FEOGA guarantee section, it will be for the Commission in the first instance to take whatever action to moderate expenditure lies within the powers entrusted to it by the Council in Regulations on the common organisation of markets. These powers currently include the fixing of export refunds and other amounts and the introduction or suspension of intervention and of other support and/or disposal measures. The examination of the issues listed by the European Council will need to cover the question whether the Commission's existing powers are adequate to enable them to observe the guideline. If such action by the Commission on its own does not appear likely to keep future expenditure within the financial framework laid down, then, thirdly, it will be for the Commission to report the situation and make appropriate proposals for corrective action to the Agriculture Council. These proposals could, depending on the situation, include a review of the decisions already taken by the Council at the annual price fixing. Only after resort to all possible measures by the Council and the Commission will the question of the need for a supplementary budget, under the

procedures set out in paragraph 13 above, arise.

D. OPERATION OF THE CAP

18. The European Council agreed at Stuttgart that adaption of the CAP to the situation facing the Community in the foreseeable future is necessary if it is to fulfil its aim in a more coherent manner. The establishment of a financial framework of the kind outlined above will, in the view of the British Government, make an essential contribution to achieving that objective. But adaptation in the operation of the Common Agricultural Policy itself will also be needed if it is to meet its purposes more effectively.

19. There will be discussion on these questions over the coming months in order to establish the "concrete steps compatible with market conditions to ensure effective control of agricultural expenditure by making full use of available possibilities and examining all market organisations" for which the Stuttgart Declaration has called. We look forward with interest to the Commission's proposals on the steps which may be necessary. The British Government considers they will need to include, among other ideas, a commitment to a sustained policy of restraint on common prices and a narrowing of the gap between Community prices for commodities in surplus and those of its principal competitors; rigorous application of guarantee thresholds designed to limit the Community's guarantee to producers by reference to the quantities which it is appropriate to produce within the Community; and other measures compatible with market conditions in the individual commodity sectors to make the policy more cost-effective.

20. Such adaption is needed from a budgetary point of view, but it is needed too, to secure the achievements of the CAP; to reduce the problems which surplus disposal can create in the Community's relations with its trading partners including those in the Third World; and to provide a more healthy basis for the future development of European agriculture.

EURO POL: Budget

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