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CABINET

MINISTERIAL STEERING COMMITTEE ON ECONOMIC STRATEGY

SUB-COMMITTEE ON ECONOMIC AFFAIRS

EUROPEAN COMMUNITY EXPENDITURE PROGRAMMES AND CONTROL OF UNITED KINGDOM PUBLIC EXPENDITURE

Note by the Secretaries

A note by the Chairman of the Steering Committee on European Questions is attached.

Signed SIR ROBERT ARMSTRONG
P L GREGSON
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Cabinet Office
28 November 1983

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EUROPEAN COMMUNITY EXPENDITURE PROGRAMMES AND CONTROL OF UNITED KINGDOM PUBLIC EXPENDITURE

Note by the Chairman of the Steering Committee on European Questions

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1. The Treasury proposals were discussed in the Steering Committee on European Questions (EQS) on 24 November. In the light of that discussion the Chancellor of the Exchequer is now submitting a memorandum to the Ministerial Steering Committee on Economic Strategy: Sub-Committee on Economic Affairs. Since a large number of Departments have an interest in these proposals, this note seeks to summarise the principal problems which those Departments identified in the EQS discussion.

Objections of Overseas Development Administration to present arrangements on aid expenditure

2. The Overseas Development Administration (ODA), as the only Department to which a full system of attribution of Community expenditure to its departmental budget currently applies, seek a change to that system. They do not wish increases in Community aid to be automatically reflected in reductions in the United Kingdom's aid programme as they see the objectives of the two programmes as being basically different. They point out that whereas Community aid programmes in the early days constituted only a small percentage of national aid expenditure the situation has now substantially changed. Community aid programmes now make up some 20% of the ODA's total expenditure (of which over half is attributed to the ODA budget, the remainder being the United Kingdom share of the European Development Fund which is voted separately). As Community aid expenditure has been growing faster than United Kingdom bilateral aid, attribution combined with cash limits has made it impossible to carry out the Government's policy of increasing the proportion of bilateral as compared to multilateral aid. Major problems of financial management also arise because Community aid is often increased at the last moment and is subject to unanticipated exchange rate fluctuations. ODA also argue that it is inappropriate to expect them to bear the cost of Community aid programmes to which the United Kingdom has agreed on wider political grounds rather than for reasons of aid policy, or which have been imposed against ODA's will by the European

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Parliament or because the UK was outvoted in the Budget or other Council. ODA are therefore seeking the reform of the system of attribution for Community aid expenditure. There are certain administrative arrangements intended to provide some flexibility but ODA does not consider them effective. Discussion between Treasury and ODA officials of possible schemes to provide ODA with a right to draw on the contingency reserve to meet unforeseen and unavoidable additional Community expenditure have so far failed to produce a scheme acceptable to all concerned.

New expenditure programmes (and non-quota receipts for the European Regional Development Fund)

3. The Government's policy in relation to existing Community expenditure programmes is broadly based on "non-additionality", ie that the Community programmes should not give rise to additional public expenditure in the United Kingdom. The Treasury does not exclude a limited element of flexibility. All other Departments see a number of strong objections to the Treasury proposal to extend the principle of non-additionality at the Departmental level to new programmes. The Department of Trade and Industry and other Departments concerned also object to the application of non-additionality to those parts of ERDF non-quota receipts which go to the private sector. They argue that Community expenditure is not comparable to other public expenditure as it is both to a large extent outside Her Majesty's Government's control and has different aims. A system of attribution or systematic off-setting savings at the Departmental level would therefore give rise in their view to:

a. Distortion of government policies. Community expenditure programmes are sometimes accepted because the United Kingdom is outvoted or for wider political and other reasons, eg because we want other member states who benefit from the programme to support something of interest to us or because we want to avoid an even more unwelcome programme in another field or in another part of the budget. In the aid field, pressure from the Third World and/or other donors can also be instrumental in causing the United Kingdom to accept Community programmes whose merits we doubt (eg to avoid headlines such as "UK blocks Community famine relief programme"). In other cases, Community expenditure of no interest to the United

Kingdom is imposed by the European Parliament. In such cases, if individual Departments had to bear the cost of the relevant Community expenditure on their own budgets, this could usually only be done by squeezing out domestic programmes to which they attach greater importance, with a resulting distortion of Government priorities. Departments therefore argue that in all such circumstances the expenditure should be accepted as part of the general price of Community membership and that any necessary offsetting savings should be found at the overall level of public expenditure rather than from individual Departments.

b. Problems of financial management. These would arise because it is difficult to control or to forecast contributions to and receipts from Community programmes over the PESC period or even for a year ahead, given:

(i) the one year time horizon of the EC budget and the weakness of existing (triennial) forecasts, and the fact that the Community's system of budgetary control does not require strict accounting of expenditure within a given financial year.

(ii) the mis-match between the PESC and Community budget timetables;

(iii) the nature of the decision-making and management procedures in the Community, which may include unavoidable changes in Community expenditure at short notice, eg because of European Parliament action, rectifying budgets or virements from another budget line. There are also problems about monitoring EC expenditure and its allocation between member states during the year, especially given the different Community and United Kingdom financial years. Fluctuation in the exchange rate is a further variable.

These uncertainties would pose (and do pose in the case of the aid programme) problems of financial management for individual Departments.

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especially in cases where Community expenditure represents a significant proportion of a particular Department's total expenditure, as domestic programmes cannot always be adjusted rapidly.

4. Departments, including the Foreign and Commonwealth Office, also advance these wider arguments:

a. Failing to maximise UK receipts. When Community programmes involve receipts going to the private sector (eg in the research field, where the beneficiaries are sometimes private establishments which would not normally be funded by Departments) Departments will have a strong incentive, to avoid cuts in their existing Departmental programme, to oppose the Community programmes for the private sector even if they involve a net financial benefit for the United Kingdom. And if any system of off-setting savings were based on receipts received (as opposed to the United Kingdom's gross or net contribution) the Department concerned would have an incentive to discourage British private sector establishments from participating, with the net effect that the United Kingdom would be making the same contribution to the programme while getting less out of it. Similarly, in the case of the non-quota section of the ERDF, the Department of Trade and Industry would have an incentive to avoid claiming benefits which they would have to pass on to the private sector, because of the cuts they would have to make in other programmes. In both cases, the policy of the Departments concerned would be out of line with Her Majesty's Government's current policy of maximising receipts from the Community. It could also be damaging in terms of United Kingdom domestic public opinion (eg if the potential non-quota benefits for small and medium sized enterprises under the European Regional Development Fund were not claimed).

b. Effect of consistently negative attitude in the Community. Departments already take a highly critical attitude towards Community programmes both for financial and other reasons. The automatic application of cuts in Departmental budgets corresponding to new Community programmes, however, could give an incentive to oppose any Community programme which did not bring them a net budgetary benefit

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regardless of its intrinsic merit. Departments argue that a consistently negative attitude to new expenditure programmes would make it more difficult to achieve our aim of channelling Community expenditure in more acceptable directions. Since in many cases the UK would not in practice be able to influence the level of expenditure, we would get the worst of all worlds.

c. Maintaining the fiction of additionality. Insofar as the Commission still insists on the additionality principle (eg under the ERDF and other regional programmes) the automatic application of off-setting savings would make it even more difficult to persuade the Commission and the European Parliament that we apply additionality. There would be particular difficulties in Northern Ireland, where the additionality of Community financing is an important political issue.

d. Extra bureaucracy. Departments claim - although this point has not been examined fully at official level - that the proposals would create new administrative burdens. Particularly in the research field, Community expenditure programmes may be of interest to two or more Departments (eg Departments of Trade and Industry and of Energy, or the different regional Departments), and in such cases it could be administratively time-consuming to allocate responsibility (and therefore financial liabilities and benefits) between Departments.

Other measures which Departments believe would be worth pursuing

5. The Treasury has already suggested ways of improving forward planning in relation to the effect of Community expenditure on domestic public expenditure ("the forward look"), which they see as complementary to, and not an alternative to, their other proposals. There is agreement of all Departments to the principle of minimising the impact of Community expenditure on domestic public expenditure. There is also agreement that, where there is a direct overlap between a proposed Community programme and a domestic programme, there should be savings in order to eliminate wasteful duplication. On this basis some Departments have suggested that, where new expenditure programmes were agreed, there should be a presumption of off-setting savings when a Community programme genuinely replaced a domestically financed one, but in all other cases the following arrangements would be applied:

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(i) Off-setting savings would be found where possible within Programme 2.7: ie the aggregate programme of UK net payments to the Community budget. Although this would be against the doctrine of not using windfall savings to increase expenditure in another area, it would have the advantage of saving the United Kingdom from having, to oppose on financial grounds within the Community, programmes which did not involve any increase in anticipated total Community expenditure.

(ii) Net increases under programme 2.7 would be offset, if necessary, at the overall level of United Kingdom public expenditure.

Signed D F WILLIAMSON

Cabinet Office

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