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INFO ROUTINE EC POSTS, WASHINGTON, UKMIS GENEVA, TOKYO

FRAME ECONOMIC

CALL ON FRG ECONOMICS MINISTER.

SUMMARY

1. I CALLED ON HAUSSMANN (FDP) ON 9 MAY. HE EMPHASISED THE IMPORTANCE OF MORE COORDINATION BETWEEN BRITAIN AND GERMANY ON EC MATTERS. HE WAS GENERALLY HELPFUL ON MONETARY UNION, CARS AND MERGER POLICY, BUT MUCH LESS SO ON WITHHOLDING TAX.

DETAIL

2. I TOLD THE ECONOMICS MINISTER THAT LORD YOUNG EXPECTED TO BE IN BONN TO ADDRESS THE CDU ECONOMIC COUNCIL ON 17 OCTOBER. HAUSSMANN RECALLED HIS MEETING WITH LORD YOUNG IN ZURICH AND DAVOS AND HOPED A MEETING WOULD BE POSSIBLE IN OCTOBER. I ALSO SUGGESTED THAT HE MIGHT LIKE TO VISIT LONDON SOON.

MERGER POLICY

3. HAUSSMANN SAID THAT IT WAS BECOMING URGENT TO HAVE AN EC-WIDE POLICY. ALTHOUGH THE GERMANS HAD AGREED TO A 500 BECU THRESHOLD, THEY SYMPATHISED WITH OUR WISH FOR A HIGHER FIGURE. HE AGREED THAT THERE SHOULD BE NO AUTOMATIC REDUCTION OF THE THRESHOLD, THAT UNANIMITY SHOULD BE REQUIRED FOR ANY COUNCIL DECISION TO REDUCE IT AND THAT THE ONLY CRITERION FOR JUDGING MERGERS SHOULD BE COMPETITION POLICY. HOWEVER, IT WAS A MATTER OF CONVINCING THE FRENCH AND ONE PROBLEM WAS THAT THREE DIFFERENT MINISTRIES WERE INVOLVED IN PARIS.

CARS

4. HAUSSMANN SAID THAT HE HOPED FOR MORE SUPPORT FROM BRITAIN IN COUNTERING FRENCH PRESSURE FOR QUOTAS AND LOCAL CONTENT RULES. THERE WAS NO CONCEPT OF LOCAL CONTENT IN THE TRADE SYSTEM OF THE EC. IT WOULD NOT BE DEFENSIBLE IN THE GATT TO CUT THE JAPANESE OFF FROM EXPORTING CARS AFTER GETTING THEM TO INVEST IN EUROPE.

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ENERGY POLICY

5. HE SAID THAT HE WAS INCLINED TO GO ALONG WITH THE COMMISSION'S POLICY OF FORCING THE FEDERAL GOVERNMENT TO CUT ENERGY SUBSIDIES.

DELORS REPORT.

6. HAUSSMANN WAS NOT IN FAVOUR OF RUSHING TOWARDS MONETARY UNION. HE PREFERRED A STEP-BY-STEP APPROACH IN WHICH MONETARY UNION WOULD BE THE CROWNING ACHIEVEMENT. HOWEVER THE COMMISSION HAD MODIFIED ITS POSITION. DELORS WAS NO LONGER INSISTING ON AN ADVANCE COMMITMENT TO THE ERM BY THE UK AND WE SHOULD RESPOND BY AGREEING TO DISCUSS THE STRUCTURE OF AN INDEPENDENT EUROPEAN CENTRAL BANK CONSTRUCTIVELY. I SAID THAT THE UK WAS NOT IN FAVOUR OF A TIMETABLE AND THAT TREATY AMENDMENT, NOT TO SPEAK OF PRIOR COMMITMENTS TO EMU, WERE OUT OF THE QUESTION. HE SAID HE SYMPATHISED ON ALL THREE POINTS BUT THAT IN VIEW OF BRITAIN'S CAPABILITY IN FINANCIAL SERVICES IT MUST BE IN OUR INTEREST TO INFLUENCE EUROPEAN CURRENCY DECISIONS. REMAINING OUTSIDE THE PROCESS WOULD PREVENT THE CITY OF LONDON REALISING ITS FULL OPPORTUNITIES. IT WAS IN OUR INTEREST TO SECURE THE FREE MOVEMENT OF CAPITAL, BUT THE FRENCH WOULD BLOCK THIS UNLESS THEIR PRECONDITIONS ON MONETARY UNION AND TAXATION WERE SATISFIED.

WITHHOLDING TAX

7. HAUSSMANN SAID THAT GERMAN EXPERIENCE WITH WITHHOLDING TAX HAD BEEN UNHAPPY. THE BANKS HAD NOT HELPED THE GOVERNMENT, AND THERE HAD BEEN AN INTOLERABLE FLIGHT OF CAPITAL. HOWEVER THE TAX HAD BEEN SUSPENDED, NOT CANCELLED. THERE WOULD HAVE TO BE A EUROPEAN-WIDE AGREEMENT ON THE MANNER OF TAXATION OF INTEREST ON CAPITAL AS A PRECONDITION FOR THE FREE MOVEMENT OF CAPITAL. ONCE LUXEMBOURG WAS INCLUDED IN THE ARRANGEMENTS, THERE WOULD BE NO RISK OF CAPITAL FLIGHT FROM GERMANY AND THE WITHHOLDING TAX COULD BE REINTRODUCED, THOUGH HE RECOGNISED THAT REPEATED REVERSALS IN TAX POLICY WERE UNDIGNIFIED. I SAID THAT, EVEN IF LUXEMBOURG AGREED TO INTRODUCE A TAX, THERE WOULD STILL BE THE RISK OF CAPITAL FLIGHT TO PLACES OUTSIDE THE EC, ESPECIALLY AS THE GLOBALISATION OF TRADE AND FINANCE PROGRESSED. HE THOUGHT THAT GERMAN SAVERS WOULD BE LESS TEMPTED TO PUT THEIR MONEY IN EXOTIC OFF-SHORE TAX HAVENS OUTSIDE THE EC.

VAT

8. HAUSSMANN AGREED THAT THE COMMISSION'S CLEARING HOUSE PROPOSAL WAS A DISASTER. THE PROBLEM WITH THE BRITISH POSITION ON

HARMONISATION WAS THAT THE MARKET SOLUTION WOULD DISADVANTAGE THE SMALL MEMBER STATES. HE DID NOT ARGUE FOR COMPLETE HARMONISATION BUT FOR TAX BANDS ALONG WITH ZERO RATED ITEMS AS A TRANSITIONAL MEASURE. ZERO RATES MIGHT HAVE TO RISE TO SAY 4 PER CENT OVER TIME. THERE COULD BE SPECIAL MEASURES FOR PERIPHERAL AREAS LIKE DENMARK AND GREECE AND PERHAPS ALSO FOR BRITAIN AND IRELAND. HE DID NOT WANT TO INCREASE PRESSURE FOR ZERO RATES IN SOCIALIST COMMUNITY COUNTRIES BY ACCEPTING THE UK ZERO RATES ON A PERMANENT BASIS BECAUSE THE SMALLER COUNTRIES HAD TO BALANCE THEIR BUDGETS AND BECAUSE FRG TAX POLICY WAS TO DECREASE DIRECT TAXATION WHILE INCREASING INDIRECT TAXATION.

GATT URUGUAY ROUND

9. I SAID THAT FURTHER COMPROMISE WOULD BE NEEDED ON AGRICULTURE. THE FRG'S INDUSTRIAL INTERESTS WERE IMMEASURABLY GREATER THAN HER AGRICULTURAL. HAUSSMANN SAID THAT GERMANY HAD ALREADY MADE CONCESSIONS AND HIS MINISTRY HAD ARGUED FOR FLEXIBILITY. HOWEVER GERMANY'S ELECTORAL SYSTEM MADE IT HARDER THAN FOR US TO INTRODUCE UNPOPULAR STRUCTURAL POLICIES. THE GOVERNMENT DID NOT WANT TO LOSE VOTES TO THE RIGHT WING REPUBLICANS. IN THE FRG EMPLOYMENT IN MODERN INDUSTRIES WAS GRADUALLY INCREASING AND THIS WOULD HELP REDUCE THE PRESSURE TO MAINTAIN JOBS ON THE LAND. HE UNDERSTOOD THE AMERICAN ATTITUDE AND SAW THE NEED TO RESPOND CONSTRUCTIVELY.

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