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MR POWELL

cc: Sir R Butler
Mr Hadley
Mr Appleyard

OD 8 MARCH: EC IMPLICATIONS OF GERMAN UNIFICATION

I attach a Chairman's brief for the Prime Minister's use at tomorrow's meeting of OD.

LYN PARKER

7 March 1990

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OD, 8 MARCH 1990: CHAIRMAN'S BRIEF

EC IMPLICATIONS OF GERMAN UNIFICATION

Paper for discussion: OD(90)3

Introduction

1. The Foreign Secretary's paper, based on interdepartmental discussion by officials, identifies the main EC implications of German unification and suggests preliminary conclusions for UK policy.

Key Issues

2. The key issues are:

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- the likely economic impact of German unification, and how far this can be influenced by the EC;
 - how to maximise UK influence over what will inevitably be an untidy negotiation; and in particular how to ensure that our key concerns are properly addressed;
 - what our policy on transitional derogations should be; and
 - how to ensure that the EC's budgetary exposure is kept to an absolute minimum.

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Economic Impact

3. The assessment in paras 4-7 of the Foreign Secretary's paper was drafted in consultation with the Treasury. You will wish to confirm that the Chancellor and other colleagues are content with the broad picture that emerges, ie that there will be heavy short term costs, mainly for the FRG, but probable longer term benefits for both Germany and the EC.

Likely negotiating process

4. The starting-point is that, on unification, EC rights and obligations will in principle automatically apply in the ex-GDR: it will be for the German Government to request such temporary derogations from EC obligations as it thinks necessary, and for member states to decide what to concede and on what terms.

5. The key issues you may wish to explore are:

- handling and timing: a tidy EC negotiation seems unlikely, for the reasons set out in paras 8-10 of the paper. The Commission have already begun work and will produce a paper for discussion at the special Dublin Summit on 28 April. We will want to ensure that the Council is fully engaged from an early stage;
- amendments to EC law: much EC secondary legislation will need to be adapted, or provision made for derogations and transitional periods (para 12). The Germans claim that Treaty amendment will be unnecessary, and it is true that technical adaptation of EC legislation, and some temporary derogations, could be made by Council decision. But any temporary derogations from the Treaty rules themselves (eg on the free movement of goods) would require formal Treaty

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provisions (and consequent national ratification procedures, which would introduce further delay). You may wish to ask the Attorney-General to comment on these issues: and then to check that colleagues agree with the suggestion in para 11 that it would in any case be preferable to wrap all the changes up in a single Treaty instrument (the tidiest solution; though a mini-IGC would be necessary, this would be quite separate from discussions on EMU, and should be a mere formality);

- implementation in the ex-GDR: colleagues may also wish to underline the importance of proper mechanisms to ensure this.

Single Market (paras 15-18) and Transport (para 30)

6. Here the key issues are:

- how to keep any transitional derogations to a minimum;
- how to maintain adequate safeguards to prevent distortion of trade while transitional arrangements continue.

Much will depend on what concessions the FRG/GDR themselves seek. There are some significant practical problems over maintaining safeguards: these will be explored interdepartmentally by officials shortly, on the basis of a detailed paper by DTI. It may be helpful that distortions of competition are likely to be of particular concern to the FRG itself, which will be the first to suffer from unfair competition from the ex-GDR. The Foreign Secretary's paper hints (para 17, last sentence) that controls at the FRG's border with the rest of the Community may be easier to achieve than controls at the inner German border, which may be

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resisted on both symbolic and practical grounds. The Secretary of State for Trade and Industry and the Foreign Secretary might be invited to comment on these issues.

Agriculture and Fisheries (paras 19-24)

7. The key issues you may wish to explore are:

- the need to ensure that technical adaptations to CAP systems (milk quotas, guaranteed quantities for cereals etc) are not used by the Germans or others as a pretext for weakening stabilisers;
- how far the likelihood of practical problems in introducing Community health and quality standards could strengthen our wider case for continuing to police trade with the ex-GDR until relevant derogations have expired;
- the implications for the EC budget (the Chancellor of the Exchequer in particular may wish to comment);
- whether all this is likely to have any significant impact on German attitudes to CAP reform.

Environment

8. This is likely to prove one of the most difficult and expensive areas for the FRG. The paper argues for short transitional periods (none at all for new plant introduced from the FRG) and that promoting UK exports in the pollution control field should if necessary take second place to our prime objective of resisting EC expenditure. You will wish to check that colleagues are content with this approach.

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Energy (para 26)

9. The Secretary of State for Energy may wish to comment. As any aid for mine closures would be financed by a levy on the EC coal industry, rather than the EC budget, we should be in a strong position to round up allies to resist any such proposal.

Social Policy (para 27)

10. The Secretary of State for Employment may wish to comment. The problems appear to be largely for the FRG to resolve.

Immigration/Frontiers (para 28)

11. Ensuring that the Community's new external frontier is adequately policed will be an important objective for the UK. In the process, some difficult security problems will need to be addressed. The Parliamentary Under-Secretary of State, Home Office (Mr Lloyd) may wish to comment briefly: the issues will need to be pursued separately at a later stage.

Customs Union, External Trade (paras 31-32)

12. The paper suggests that the Germans may seek a transitional period before a full customs union, to smooth the reorientation of the GDR's existing trading pattern away from COMECON and towards Western Europe. You may wish to note that any delay in introducing full customs union will again raise the question of controls at the inner-German border or the German border with the rest of the EC: all this will require further study.

State Aids and Competition Policy (paras 33-34)

13. The paper argues that we should resist transitional arrangements in this area, and press for German state aids and other arrangements restricting competition to be dealt with under the normal Treaty rules. We shall also be arguing against the

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provision of financial help by the EC. You may wish to probe how far we can expect to achieve both these objectives.

Structural Funds (paras 35-37)

14. This is likely to prove a major area of difficulty in the negotiations, given the significant potential budgetary implications. The Secretaries of State for Trade and Industry, Employment and Environment all have an interest, as does the Chancellor of the Exchequer. You will wish to invite their comments on the analysis and recommendations in the paper.

Budget (paras 38-41)

15. The paper gives some indicative figures for the range of contributions and receipts which might be attributable to the ex-GDR. The net increase in the UK's annual contribution after Fontainebleau abatement would be much smaller than those for France and Italy. Even after taking account of net receipts for the GDR, the Germans would remain much the largest contributors overall. These changes in the pattern of contributions could add fuel to pressures to reduce the UK's Fontainebleau benefits when the arrangements come up for review in 1992. You may wish to invite the Chancellor of the Exchequer to comment on the Foreign Secretary's analysis, and on the prediction (para 41, last sentence) that GDR integration could almost certainly be accommodated within the existing own resources ceiling until 1992, and possibly for some years thereafter.

Institutional Consequences (para 42)

16. The paper suggests that the Germans' prime interest is likely to be in securing greater representation in the European Parliament, though not straight away. You may wish to check that colleagues agree with this analysis.

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Conclusions

17. The conclusions suggested in para 43 are closely based on the analysis earlier in the paper. You may wish to establish that colleagues are content to proceed on this basis. The Foreign Secretary may suggest that the next step should be to seek privately to influence the Presidency and Commission as they prepare for the Dublin meeting which you will be attending on 28 April.

Cabinet Office

7 March 1990