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CHAIRMAN'S BRIEF: OD, 27 MARCH 1990

GERMAN UNIFICATION

Papers for discussion: (i) Derogations and safeguards

- OD(90)6 (trade)
- OD(90)7 (agriculture)
- OD(90)8 (other sectors)

(ii) Budgetary implications

- OD(90)10

(iii) Tactics

- Foreign Secretary's minute of 23 March

PURPOSE

1. You may wish to begin by establishing our objectives on derogations/safeguards; then note the Chancellor's updated projection of the possible budgetary costs; and finally discuss the tactical issues in the Foreign Secretary's minute and the other papers.

DEROGATIONS AND SAFEGUARDS

2. Here there are four key issues on which you may want to focus:

(i) what are the trade risks in the period before unification, and what do we need to do about them?

Mr Ridley is concerned that the longer unification is delayed, the greater the risk of unfair competition from modernised East

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German production. Colleagues may agree that:

- the FRG must continue to police inner-German trade vigorously to ensure that the requirements of the EC Treaty are fully observed;
- if significant problems of leakage occur, we should press the Commission to take appropriate action with the German authorities;
- in the last resort, we should be ready to take national safeguard action, as the Treaty allows.

(ii) after unification, what trade safeguards will we need while there are derogations from full application of EC rules?

Mr Ridley argues that border controls are irrelevant to tackling unfair pricing, which will arise at the point of sale. You will want to confirm that colleagues agree with his conclusions that:

- realistically, some derogations are inevitable; but we should keep them as short and limited as possible, and ensure that they are subject to close monitoring by the Commission;
- if continuing controls at the Inner German Border are required for other reasons (eg agriculture) there may be scope for using them for safeguard purposes as well, but we should not rely solely on this route;
- the most effective safeguard is likely to be a dispute settlement procedure allowing aggrieved parties to complain

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to the Commission about unfair pricing, and the Commission to impose remedies on the offending FRG firm;

- in any event, EC state aid and competition rules should be applied from the outset.

(iii) after unification, what safeguards may be needed for agriculture until CAP rules apply fully?

Mr Gummer's paper starts from the fact that the CAP will apply automatically in East Germany as soon as unification takes place, subject to whatever transitional arrangements are negotiated.

There seem to be three broad possibilities:

- if East German producer prices start higher than in the rest of the EC, bringing them into line over a transitional period would involve extra cost to the EC budget; we and other member states would clearly need to resist such an approach;
- if producer prices start lower than in the rest of the EC, and the Germans wish to bring them into line over a transitional period, there could be net savings to the EC budget; but a short transition period and an effective control régime at the inner German border would then be essential (the West Germans would want the latter too, to protect their market from being undercut by cheap East German produce). In addition, there seems no reason why Mr Ridley's idea of a dispute settlement procedure should not extend to agricultural trade: you may wish to confirm this;
- in theory, East German producer prices could be brought into line with CAP prices immediately, in which case border

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controls would not be needed; Mr Gummer's paper implies that this is not very likely, while the Foreign Secretary's minute (para 5) implies the reverse. You may wish to explore this further.

In addition, OD may wish to:

- note that permanent adjustments to CAP régimes (eg milk and sugar quotas) will need to be watched closely to keep FEOGA costs to a minimum;
- agree that, where the GDR has long-term commitments to agricultural exports (eg to the USSR) Germany should pay any subsidies in excess of normal EC export refunds;
- note that derogations permitting East German products which do not meet EC standards to circulate within East Germany, or perhaps a united Germany, should be acceptable; but we should resist derogations aimed at the free circulation of such goods in the rest of the Community;
- agree that, on plant/animal/fish health, we should strongly resist any request for derogations which would weaken existing controls against the movement of disease.

(iv) which other fields are likely to be of special concern to the United Kingdom?

The paper by the Secretaries suggests that in other areas the United Kingdom's prime interest in derogations/safeguards is likely to be over energy and the environment (where other member states are likely to share our concerns); and that there may be

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some bilateral leverage with the FRG over road haulage liberalisation.

You may wish to suggest that officials should look in more detail at the environment (including nuclear) issues.

BUDGETARY IMPLICATIONS

3. OD may wish to note the Chancellor's paper, which simply updates the assessment in the Foreign Secretary's paper for the last meeting, and does not call for any action at this stage. The main change is a substantial downward revision of the likely cost when East Germany eventually becomes eligible for assistance from the structural funds.

TACTICAL ISSUES

4. Finally, you may wish to focus on the tactical issues arising from the three main papers. The key points seem to be:

- we must ensure that the Germans remain the demandeurs: this is our strongest negotiating card;
- other member states will share most of our concerns: we should not allow them to sit back and leave us to make all the running;
- the Foreign Secretary suggests that our aim at the 28 April Summit should be agreement on the right Community framework and procedures to suit our interests;

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- the Foreign Secretary also recommends that:
  - your line with Chancellor Kohl should be that once the Article 23 decision is taken, the objective should be to integrate the ex-GDR in the Community as fully and quickly as possible;
  - we should not press, at this stage, for continued controls at the inner-German border after unification, though the need for these will have to be kept under review; but we should underline the importance of securing the Eastern border of the ex-GDR;
  - the safeguards issue should be pursued with the Commission on the lines recommended by Mr Ridley;
  - we should also compare notes with other member states (particularly the French, Italians, Dutch and Spanish) with a view to forming alliances.

Finally, you may wish to conclude that OD may need to return to this subject once German intentions are clearer.

Cabinet Office

26 March 1990