Qz.03616

MR COLES

PREPARATION FOR THE EUROPEAN COUNCIL OF 19-20 MARCH

A meeting of Ministers has been arranged for 7 March in order to review the state of the post-Stuttgart negotiations in preparation for the European Council of 19-20 March. I attach a paper which has been prepared by the European Secretariat of the Cabinet Office, after discussion with Departments, as a basis for discussion at the meeting on 8 March.

I am sending copies to Roger Bone (FCO), John Kerr (Treasury), Ivor Llewelyn (MAFF) and to Sir Robert Armstrong.

D F Williamson

D F WILLIAMSON

5 March 1984

FUTURE FINANCING AND DEVELOPMENT OF THE COMMUNITY

PREPARATION FOR THE EUROPEAN COUNCIL

Note by the European Secretariat, Cabinet Office

Background

1. The major issues for these negotiations were set out by the European Council in its declaration at Stuttgart on 18 June 1983 (text at Annex I). The failure in December of the Athens European Council to reach any conclusions has not changed the agenda established at Stuttgart but the French Presidency which took over from the Greeks on 1 January has considerably changed the nature of the negotiation which has proceeded mainly by bilateral contacts with little multilateral negotiation and with few new documents made available in the Community. In particular,

(i) the main questions for the European Council will be the central core issues of the future financing of the Community - correction of the budget inequity, control of agricultural and other spending, the size of own resources. If there is agreement on these points, there will probably also be a further declaration on the timing of the Community's enlargement;

(ii) some agricultural questions will almost certainly be remitted to the European Council - in particular monetary compensatory amounts (MCAs) and means of controlling milk production (the super levy). Discussions on a wide range of agricultural questions are going on in the Agriculture Council together with the 1984 price fixing. We need to ensure that potential solutions do not get out of step. We cannot be sure, however, which of the many agricultural problems the Presidency will decide to submit to the European Council.

(iii) new policies are being dealt with, as far as possible, in the normal Councils. We expect, however, that they will form a part of the communique from the next European Council and that this part of the negotiation will not be controversial.

2. The French Presidency is planning that any agreement or substantive progress reached at the European Council on 19/20 March would be on the major issues only, with the various legal and other texts being worked up for approval

by the June Council. This is not against our interest provided that we ensure that the financing package is held together and that any text on own resources is made subject to exactly the same conditions as any text on the correction of the budget inequity and the control of spending. The implementation of any agreements on the three questions would have to proceed strictly in parallel. We cannot accept any increase in own resources without including in the same package the legal and other texts necessary to satisfy the conditions which the Prime Minister laid down at Stuttgart.

3. This note covers:

I.	Correcting the budget inequity	(paras 4 to 16)
II.	Budgetary discipline	(" 17 " 20)
III.	Own Resources	(" 21 " 22)
IV.	Agricultural issues	(" 23 " 24)
V.	New policies	(" 25)

I. Correcting the budget inequity

4. This is the central issue for the United Kingdom. It is the price which other member states now have to pay because without it there will be no agreement on an increase in own resources. The present level of own resources is not sufficient to finance existing agricultural and other programmes in 1984 and 1985, and various expendients to reduce or defer expenditure are being pursued by the Commission. Although a number of suggested solutions to the budget inequity were put forward last year and none have been withdrawn, it seems to us that in practice the negotiation is now focussed on three forms of a safety net:

(i) the United Kingdom's proposal for setting a limit on net contributions related to ability to pay:

(ii) the outline German scheme advanced at Athens, which also sets a limit related to ability to pay but based on the VAT share/expenditure share gap, which in the United Kingdom's case is less than the net contribution;

(iii) a French scheme on similar lines to the German but with various devices for removing the benefit to Germany and reducing the benefits to the United Kingdom which would leave us with a high net contribution after adjustment.

These schemes are described in Annex II. The Commission may also put forward a proposal on the lines of (ii) above. Many member states are just as concerned about minimising benefits to Germany as they are about the adjustment of the British contribution.

5. We have made progress in persuading most member states that

- there must be a system of budgetary correction, based on a member state's relative prosperity and exprssed as a percentage of its gross domestic product;

- this sytem is to be included in the own resources decision and to last as long as the problem lasts;

- the correction must be made on the revenue side by reducing a member state's VAT contribution in the following year;

- the correction of the budget inequity should come into effect in 1985 so that it could apply to our relief for 1984. The Germans, however, are opposed to any increase in own resources before enlargement (ie 1 January 1986 at the earliest).

On the figures which should result from the system, however, there is at present a very wide gap between the United Kingdom's position and the proposals which the French Presidency is likely to put forward. The difference can be broadly expressed as follows: the United Kingdom has stated that it could agree to make an adjusted net contribution of 450-500 million ecu (based on 1982 figures and using the relative prosperity of a Community of 12) while the French Presidency may propose that the United Kingdom's adjusted net contribution should be of the order of 1200-1300 million ecu. This gap has to be closed in our favour.

6. Although some major elements in the United Kingdom's safety net proposal are likely to be accepted in a revised financing system, almost all member states have opposed the concept of net contributions, which they reject on principle and because it maximises our budgetary claim. We need now to judge whether we can obtain a safety net giving us the reduced net contribution which we seek on a reliable and sustainable basis, while accepting some changes of presentation. If the illustrative example in the paper had applied in 1982 or 1983 and using the relative prosperities of member states in a Community of 12, the results would be

	Million ecu UK 1982	1983
Unadjusted net contribution	2036	1913
(for informaiton) United Kingdom adjusted net contribution if we obtained two-thirds relief, as under ad hoc arrangements	679	638
Safety net limit on net contribution	437	525
Amount of reliefs	1599	1388

7. The figures for the net contributions of France, Germany and the United Kingdom before and after reliefs would be

	Million ecu France 1982	1983	Germany 1982	1983	United Kingdom 1982	1983
Unadjusted net contribution (- implies net benefit)	19	-5	2086	2300	2036	1913
Adjusted net contribution after reliefs (using VAT financing key)	736	608	2118	2311	437	525

In both 1982 and 1983 the German adjusted net contribution (like the United Kingdom's) is limited to the threshold established by the safety net formula. France's adjusted net contribution could be reduced slightly by using a special financing key so that their figure was about the same as ours.

8. The main differences between the German and French schemes and our own are:

(i) both these schemes are based on the VAT share/expenditure share gap and not on net contributions as they have been measured for refund purposes so far. This reduces the United Kingdom's apparent burden and by about 340 mecu on average over 1979-1983, but by between 250 and 300 mecu in 1982 and 1983;

(ii) both include a "ticket moderateur" whereby a member state whose measured gap is above its threshold would still make a marginal contribution to the excess. In the French proposal, that contribution would be very high (currently 45%);

(iii) the French proposal would redefine the allocated budget by treating administrative expenditure in a way which would reduce the United Kingdom's apparent burden and thus eligibility for relief by about 100 mecu a year. We doubt, however, whether they will insist on this.

(iv) the French proposal is constructed with the intention of giving no relief to Germany.

9. The effect is to increase by comparison with out safety net proposal the United Kingdom's net contribution after adjustment. The German proposal using the percentages in our own threshold formula, would still increase our adjusted net contribution from 437 million ecu in 1982 under the safety net to about 755 million ecu. The French scheme would be even less favourable: the United Kingdom's adjusted net contribution in 1982 would have been about 1300 million ecu (against 437 million ecu). The French themselves like to express the result in terms of relief for the United Kingdom and refer always to a proposed relief of 750 million ecu which implies an adjusted net contribution of 1200-1300 million ecu on 1982 and 1983 figures.

10. The three schemes described are not necessarily the only ones that will be on the table at the March European Council. Although we continue to stress that the United Kingdom is prepared to remain a modest net contributor and that the correct approach is to consider the net contributions after adjustment, other member states continue to think primarily in terms of the amount of reliefs for the United Kingdom. The French tactics have been to try to persuade the Germans

to rely for their own protection mainly on the favourable effect of better control of spending and by this means to weaken German pressure for a limit on net contributions and to detach the Germans from the United Kingdom position. The more the French can do this, the more they can create a common front of all other member states to hold down the benefits for the United Kingdom. Ministers will wish now to consider how best the United Kingdom can secure its aim on figures and a defensible system.

11. The four points which will particularly affect the resulting figures are:

(i) Calculation of the budget correction. The VAT share/expenditure share gap is most likely to command general support within the Community. Paragraph 12 below discusses how we should deal with this.

(ii) The "ticket moderateur". It may prove difficult to resist this altogether, since other member states claim that without it the United Kingdom would lose interest in controlling Community expenditure (since we would be compensated in full for any resulting increase in our net contribution). A 5% ticket moderateur would cost about 65 to 75 million ecu.

(iii) Redefining the allocated budget. We should be able to continue to resist the proposal to reduce the size of our apparent burden by altering the way administrative expenditure is dealt with.

(iv) Net financing. We will want to continue to insist that we do not contribute to our own or to German reliefs. This will be a difficult issue in the negotiations: the prime objective of many member states is to make sure that the Germans do contribute to their own and to British reliefs.

12. Ministers will need to consider whether, provided the figure is right, the United Kingdom should be prepard at the end of the negotiations to accept a scheme based on the VAT share/expenditure share gap. Linked with this are two questions:

- how to ensure that we obtain sufficient relief under such a scheme?

- are the risks of the scheme significant?

13. In any event, the United Kingdom should continue to argue for a safety net based on full net contributions until a very late stage in the negotiations at the European Council. The discussion at the European Council is likely to focus first on the figures. If a satisfactory settlement on figures appears to be within reach, this would be the stage at which to decide whether or not to agree that the scheme should be based on the VAT share/expenditure share gap.

14. Because the measured gap is smaller, a system of reliefs based on the VAT share/expenditure share gap has to give reliefs for a higher proportion of the gap if it is to produce the same adjusted net contribution as our own proposal. In short, we would have to accept that the VAT share/own resources share gap element of our net contribution would not be subject to adjustment and accordingly we would need a high level of compensation for the rest of our net contribution. There are a number of ways in which we could tackle the situation eg:

(i) by finding some other device to top up the reliefs for the United Kingdom. One such would be to allow any member state benefiting from the corrective mechanisms and whose share of levies and duties was larger in turn than its VAT share (ie the United Kingdom) to have a correction to the latter gap as well. Since this would be our full net contribution under another name, it would produce for the United Kingdom the same result as our safety net proposal. Its only advantage for other member states is that it does not refer specifically to net contributions. An alternative would be a revised and simplified form of "Dublin mechanism" shorn of all its restrctions and constructed in such a way as to give reliefs only for the United Kingdom.

(ii) by altering the operation of the system so as to combine an increase in the United Kingdom's eligibility for reliefs with a low level of relief for Germany. This is the course which is most likely to be negotiable in the Community.

15. By such changes a scheme operating on the VAT share/expenditure share gap can be devised which would leave the United Kingdom with an estimated net contribution of around 500 million ecu (on 1982 figures with relative prosperity in a Community of 12). It should be noted, however, that the difference between the United Kingdom's net contribution and the VAT share/expenditure share gap varies from year to year. Although the gap averaged about 340 million ecu between 1979 and 1983, it has varied from 442 million ecu in 1980 to 251 million ecu in 1982. Such fluctuations mean that in some years the result will be worse than expected while in others it will be better.

16. On the correction of the budget inequity, therefore, Ministers are invited:

(i) to agree that the United Kingdom should continue to insist that there must be a revised financing system to be included in the Own Resources Decision and containing the following elements:

- a limit based on relative prosperity and expressed as a percentage of a member state's GDP;

- corrections through reductions in the VAT contribution in the following year ("on the revenue side");

- the corrections should be made from 1985 to apply reliefs for 1984.

(ii) to decide whether the United Kingdom should be ready to consider a scheme based on the VAT share/expenditure share gap, provided that the estimated adjusted net contribution resulting from it was satisfactory. This implies that the margin on the negotiation of the threshold would be tight and any "ticket moderateur" would have to be low.

II. Budget Discipline

17. The United Kingdom tabled its own proposal for a strict financial guideline to ensure that the rate of growth of FEOGA guarantee expenditure would be markedly lower than the rate of growth of own resources. The chief elements of the United Kingdom's proposal are:

(i) that the Community's budgetary procedures should embody the strict financial guideline;

(ii) that the guideline would constrain the Community's decision making procedures on the Common Agricultural Policy by limiting the amount of money available to a sum at or below the maximum permitted by the guideline;

(iii) that, if expenditure exceeded the maximum permitted by the guideline because of unforeseen circumstances, any such excess should be clawed back the following year.

The effect of these procedures would be to ensure that over a period of years the trend rate of increase of agricultural guarantee expenditure laid down in the financial guideline would not be exceeded. Many member states remain opposed to a guideline on agricultural expenditure alone. We have taken the view, therefore, that our best chance of securing our principal aim of a strict financial guideline on agricultural expenditure is to seek to incorporate it within a broader framework as proposed by the French. Accordingly at Athens, the Prime Minister tabled our own amendments to the French proposal (Annex III).

18. Since Athens, the Commission has tabled a further paper on budget discipline and the French have been taking a tougher line. At La Celle St Cloud they welcomed the Commission's revised proposals on agricultural expenditure but criticised the latest text on overall budgetary control as too lax and likely to lead to conflict between the institutions. There is a reasonable sprospect that, after further discussion in COREPER, the French Presidency will, at or before the next European Council, come forward with a text which may come close to being acceptable or at least provide the basis for a satisfactory result. We have continued, however, to press for all the main elements of our original proposal and, in partcular, that:

- the rate of growth of agricultural sending should rise markedly below the rate of growth in own resources;

- this must be included in the budgetary procedures of the Community.

It is important that the guideline for agricultural expenditure should be reliably defined and also that the Commission should respect the guideline. If the Commission never make proposals above the guideline it would require unanimity in the Council to go beyond it, so that we would have an effective veto.

19. In the final stages of the negotiations the United Kingdom's primary aim is to secure binding control of agricultural guarantee expenditure to be incorporated in the Community's budgetary procedures in a form which will determine the decisions taken at the annual price fixing. The United Kingdom should also continue to seek a commitment to a wider agreement on financial discipline for all Community spending, the terms of which should be respected by all three institutions of the Community. The best way of doing this would be by Treaty amendment (a view shared only by the French) but it would also be possible,

with the agreement of the Parliament, to achieve most of what we require by Council regulation. Even if member states could be persuaded to consider Treaty amendment, they would not wish to broach the subject openly in advance of the elections to the European Parliament in June. Our aim, therefore, should be to ensure that the substance of the agreement at the March European Council is satisfactory and that it states firmly that the agreement is to be incorporated into the budgetary procedures of the Community in a way which would permit us later to insist on the appropriate legal form, not excluding the possibility of Treaty amendment.

20. We shall need in the final stages of the negotiations to decide whether to continue to insist that the agriculture guideline should be for the rate of increase in FEOGA guarantee expenditure to be "markedly below" the rate of growth of own resources, rather than "below" the rate of growth of own resources. We have received no support for our wording but it should be possible in the end to obtain greement of all member states to "below".

III. Own Resources

21. The Government has made it clear both in the Community and in the House of Commons that the United Kingdom is only prepared to consider an increase in the Community's own resources provided that agreement is reached on:

- a more equitable arrangement for the sharing of budgetary burdens between member states, and

- strict budgetary control of agricultural and other expenditure.

22. The Commission are proposing that the ceiling on VAT contributions should be raised from 1% to 2%. There is no clear consensus among member states, though most are prepared to go to at least 1.6%. The Germans, however, have said that they will only go as far as a VAT ceiling of 1.4%. We should continue to base ourselves on the Stuttgart declaration and to discuss neither the principle nor the size of an increase in own resources until the remaining issues in the package (in particular the strict financial guideline and the figuring on the correction of imbalances) have been subject to satisfactory offers by other member states. If a satisfactory package is offered and the conditions which the United Kingdom has imposed are met, we should be prepared also to accept a revised VAT ceiling of 1.4%.

IV. Agricultural Issues

23. Most agricultural issues are now being discussed in the Council of Ministers (Agriculture) as part of the negotiations on the 1984 agricultural price fixing. There are two further meetings of the Agriculture Council before then European Council (on 5/6 March and 12/13 March). It is still not clear which issues will be put before the European Council. A meeting of the Ministerial Sub-Committee on European Questions of the Defence and Oversea Policy Committee (OD(E)) has been arranged for 8 March to discuss the outstanding qustions on the price fixing. The Defence and Oversea Policy Committee (OD) considered the United Kingdom line on the proposed supplementary levy on milk at OD(84)3rd meeting.

24. In general, the United Kingdom's position is to urge the need for a rigorous price policy, and to implementation of effective guarantee thresholds for all sectors which are, or are likely to be in surplus,where costs are increasing rapidly or where production is outrunning economic outlets, as the practical means of bringing the rate of growth of agricultural expenditure markedly below the rate of growth of the Community's resources, and to do so in a way which does not discriminate against United Kingdom producers. In the price fixing discussion we are

continuing to press for price reductions on some products and are resisting any suggestion for more generous price increases than the Commission have proposed. Ministers may wish at this stage to note the following on issues which might come to the European Council.

(i) Milk. OD agreed at OD(84)3rd meeting that it was essential for the Community to take action to deal with the surpluses and costs of the milk sector and that the supplementary levy was the least unattractive option which was likely to be negotiable and effective in tackling the problem. It concluded that the United Kingdom should continue to pursue the line that we would be prepared to consider the supplementary levy provided that it was legal, workable and non-discriminatory, and that the United Kingdom should oppose any exemptions and should work for a system operated at the farm level by reference to deliveries in 1983. The main issues will be the volume of milk above which the levy would apply (we favour the Commission's proposal of 97.2m tonnes), whether this limit should be phased in over two years and the various requests for exemptions and exceptions.

(ii) Monetary Compensatory Amounts. This has been a major point of dispute between the French and the Germans. The French are keen to phase out positive German MCAs as soon as possible. The difference between the French and the Germans is narrowing and the Germans may be prepared to suggest the following schedule for dismantling existing MCAs

(a) an immediate 3% "switch over" by reducing all positive MCAs by 3% and increasing negative MCAs to the same extent. The cost of this would depend on how quickly negative MCAs would be phased out.

(b) a commitment to remove 5 percentage points in German positive MCAs probably from 1 July 1985. This would involve a drop in prices paid to German farmers which the Germans would compensate at some cost (they say 2000M DM) to the German budget by adjustments in the arrangements by which German farmers pay VAT. This would not affect prices elsewhere in the Community.

(c) the remainder would be dismantled in line with the eixsting "Gentleman's Agreement" in the course of 1986 and 1987.

It is clear that the cost of the switch over will depend on how quickly the new negative MCAs are phased out. The United Kingdom will therefore need to concentrate on trying to get any advantages to Italy, France and Greece netted off against the Commission's price proposals. It will also be necessary to look carefully at the rules governing the creation of new MCAs following any future currency realignments, since the Germans and French will want these to be only negative and thus to involve potential costs for the Community budget. We also need to ensure that floating currencies should not automatically be subject to the same rules as currencies with fixed exchange rates and to protect our own position on this point.

(iii) Cereals and Cereal Substitutes. The United Kingdom has been seeking a Community commitment to a progressive narrowing of the gap between Community cereal prices and those in other producer countries over the next five years. Strengthening of the dollar has, however, brought American prices closer to Community prices. Nevertheless a reduction in cereal prices is essential to ensure a better cereal/livestock balance and should be argued for on that basis.

If satisfactory decisions are taken on milk and cereals, the United Kingdom is ready to authorise the opening of negotiations under Article XXVIII of the GATT with the United States and other principal suppliers with the aim of stabilising the Community's imports of corn gluten feed. Only when the results of any negotiation have been reported to the Council will the Council be required to decide whether to unbind the tariff. Our aim is to avoid provoking American retaliation and to ensure that definitive decisions are not taken before those on other parts of the package.

(iv) Oils and fats tax

The United Kingdom in common with a number of member states remains opposed to an oils and fats tax. The proposal for such a tax may effectively be dropped before the European Council.

V. New Policies

25. This was the section of the draft conclusions for the Athens Council which was nearest to agreement. The priorities put forward by the United Kingdom were the creation of a true common market for goods and services, including simplication of frontier facilities, liberalisation of transport, and a genuinely liberal insurance regime; the regeneration of industry, in particular through more effective action in research such as ESPRIT and through increased industrial collaboration- a Community solid fuels policy; and a firm timetable for the introduction of unleaded petrol. All of these were reflected in the draft on the table at Athens, and the United Kingdom has taken every opportunity since to stress to our partners the importance we attach to new policies figuring on the agenda at the March Council. Our aim is to show that the Community should look beyond narrow budgetary and agricultural issues and work constructively to develop cooperation in all areas where Community action is more effective than action on a national basis without necessarily incurring extra expenditure. We continue to stress the need for cost-effectiveness.

Conclusions

26. Ministers are invited:

(i) to agree that the United Kingdom should continue to insist on a revised system for Community financing on a lasting basis to be included in a revised Own Resources Decision and containing the elements set out in paragraph 5;

(ii) to decide whether they would accept that it should be based on the VAT share/expenditure share gap provided that the other elements of the system and the resulting figures were satisfactory (para 16);

(iii) to agree that a strict financial guideline for agricultural guarantee expenditure requiring that the rate of growth of agricultural expenditure should be markedly below the rate of growth of own resources must be incorporated in the Community's budgetary procedures; and that an agreement on overall budgetary discipline is also required in a form that does not exclude subsequent Treaty amendment (paras 19 and 20); and that all three without

(iv) to confirm the Government's position on the size of the increase in own resources (para 22);

(v) to note the position on the various agricultural issues (para 24); and on new policies (para 25).

Cabinet Office
5 March 1984

ANNEX I

DECLARATION

adopted by the European Council

in Stuttgart on 18 June 1983

At a time when the European Community is faced with enormous social and economic challenges and is in the process of negotiating a third enlargement ten years after the first accession, the European Council has decided to take broad action to ensure the relaunch of the European Community.

In the course of the coming six months a major negotiation will take place to tackle the most pressing problems facing the Community so as to provide a solid basis for the further dynamic development of the Community over the remainder of the present decade.

With regard to the importance, complexity and linkage of the problems, negotiations will be started under a special emergency procedure. For this purpose special Council sessions will take place at the level of Foreign Ministers and Finance Ministers; where necessary, other Ministers will also participate, especially Ministers of Agriculture. State Secretaries may assist the Ministers.

The result of the negotiation will be submitted to the European Council meeting in Athens on 6 December 1983.

.../...

The negotiation will cover the subjects mentioned in the conclusions of the European Council of 21-22 March 1983: the future financing of the Community, the development of Community policies, the issues relating to enlargement, particular problems of certain Member States in the budget field and in other fields and the need for greater budgetary discipline.

Decisions will be taken in common on all these questions at the end.

The negotiation will aim at examining all the existing policies with particular attention to the common agricultural policy.

The examination of policies will take place with the purpose on the one hand of modernizing and making more effective the existing policies and to determine the priority areas for new Community action, and on the other hand to ensure that policies are cost effective and that economies are made wherever possible.

The negotiation will in addition aim at a more balanced and equitable situation, also in financial terms from the point of view of the interests of the different Member States and of the Community as a whole.

The negotiation will be based on the following guidelines:

ne ommon Agricultural Policy

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. The Common Agricultural Policy must be adapted to the situation facing the Community in the foreseeable future, in order that it can fulfill its aims in a more coherent manner.

The following questions will in particular be examined:

- price policy,
- thresholds for guarantees, in relation to objectives for production
- co-responsibility of producers,
- intervention arrangements,
- arrangements on export refunds,
- substitutes and Community preferences,
- compensatory amounts,
- aids and premium arrangements,
- internal barriers to trade,
- type and size of farms, and particular situations of the various categories of farmers,
- the need for strict financial guidelines,
- external agricultural policy.
- special problems arising in certain regions, such as in the Mediterranean regions, in mountain areas or other regions at a disadvantage because of natural or economic features.

The examination will result i.a. in concrete steps compatible with market conditions being taken to ensure effective control of agricultural expenditure by making full use of available possibilities and examining all market organizations.

All Member States must contribute to achieving the savings.

Proposals will be submitted by the Commission by 1st August 1983.

The European Council has taken note of the communications of the Commission on Integrated Mediterranean Programmes which aim in particular at modernizing Mediterranean Agriculture and its better integration into the general economy. It asks the Council to examine them as soon as the Commission's proposals are submitted.

Other policies

Development of policies and new Community action

The European Council is determined to develop and make more effective Community action in research, innovation and the new technologies with a view to facilitating cooperation between enterprises. On the basis of proposals by the Commission, decisions will be taken on new Community actions making use of the Community dimension to improve the international competitiveness of enterprises.

Negotiations on certain projects of an exemplary nature, e.g. the ESPRIT programme, should be concluded as soon as possible. Likewise concrete progress should be made toward uniform standards and norms.

The protection of the environment, employment policy, in particular concerning young people and social policy will be given equally high priority.

Budgetary discipline

Expenditure must also be controlled, in cooperation with the European Parliament, outside the agricultural sector. Policies are to be developed within the bounds of financial feasibility and supplemented through new actions which must be incorporated in an economically suitable way into Community policies.

By 1st August 1983 the Commission will present a report with proposals for increasing the effectiveness of the Community's structural funds (the Regional Fund, the Social Fund and the Guidance Sector of the EAGGF). It will concentrate on a more consistent co-ordination of policies to avoid duplication of effort and expenditure and to achieve greater budgetary discipline.

On the basis of this report, the policies in question will be reviewed and priorities determined on the basis of urgency and importance.

<u>Own resources and particular problems of certain Member States</u>

The objective is:

- to secure the financing of Community policies and actions and their further development over a longer period of time taking into account the additional financial requirements which would flow from the accession of Spain and Portugal, while exhausting all posibilities for savings ;
- to agree measures which, taken as a whole, will avoid the constantly recurrent problems between the Member States over the financial consequences of the Community's budget and its financing. All appropriate ways and means will be examined to this end, in particular the proposals made by the Commission and the suggestions of certain Member States with a view to ensuring equitable financial situations for all Member States.

On the basis of the conclusions reached on development of policies, improving budgetary discipline and the examination of the Financial System, the extent and timing of the Community's requirements in terms of Own Resources will be determined.

Sound financial management

The Court of Auditors of the European Community will be asked to review the sound financial management of Community activities and to submit a report by the end of 1983. This report will be followed up in the Court's Annual Reports.

Enlargement

The accession negotiations with Spain and Portugal will be pursued with the objective of concluding them, so that the accession Treaties can be submitted for ratification when the result of the negotiation concerning the future financing of the Community is submitted.

ANNEX II

PROPOSALS FOR CORRECTION OF BUDGET INEQUITY

(i) The United Kingdom Safety Net Proposal

1. Under this proposal, the maximum net contribution which a member state would be expected to pay into the Community budget would be related to that member state's relative prosperity and to its GDP. If the member state's net contribution in any year exceeded this threshold, it would receive in the following year an abatement to its contributions to the Community budget in that year equal to the full amount of its excess net contribution in the previous year. The main features of it are:

(a) the threshold would be calculated by reference to the full net contribution to the Community's allocated budget as currently defined;

(b) in the illustrative example put forward by the United Kingdom the threshold would be set at 0 for a member state whose relative prosperity was at or below 90% of the Community average (ie a member state at or below this level would not be expected to make any net contribution). Above this level, the threshold would rise by 0.007% of the member state's GDP for each percentage point increase in its relative prosperity;

(c) the member state would receive 100% relief for all the excess of its net contribution above its threshold;

(d) the abatements would be financed by an increase in the contributions of other member states (up to their own threshold) either in proportion to their own VAT shares (the VAT financing key) or in accordance with some special financing key designed to produce a particular result;

(e) no member state would be expected to contribute to its own relief or to the relief of another member state if by so doing it would increase its net contribution above its threshold. This is known as 'net' financing.

/(ii)

(ii) The German proposal advanced at Athens

2. This proposal would also establish a safety net related to ability to pay, but:

(a) The burden would be measured by the difference between a member state's share of Community VAT (in the United Kingdom case, averaging between 20% and 21%) and its share of the receipts from the Community budget (in the United Kingdom case, about 13%) and not by the whole net contribution. This is known as the VAT share/expenditure share Gap. For the United Kingdom this gap was 1785 million ecu in 1982. On average in 1981-83 the gap was about 1512 million ecu pa about 280 million ecu less than our unadjusted net contribution. This relief therefore relates to by far the bigger part of our budget inequity, which is the low level of our receipts from the Community. But it does not cover the smaller element which results from the high volume of duties and levies transferred as own resources by the United Kingdom to the Community. It also needs to be noted that for both France and Germany the gap between VAT and expenditure is significantly larger than their net contribution, and thus exaggerates their problem. This makes it more difficult to find equitable solutions based on this gap.

(b) A member state would only be compensated for part of the amount by which its VAT share/expenditure share gap exceeded its threshold. The rate of compensation would fall with increasing relative prosperity. Every member state would therefore continue to make a marginal contribution to additional Community expenditure. This is known as a "ticket moderateur".

The German proposal contains no figures. In private, however, the Germans indicated last year that the sort of figures they had in mind would have given a relief of about 1100 mecu under their scheme in 1982. If, however, the threshold formula was the same as in the United Kingdom's safety net and if the United Kingdom contributed 5% to expenditure above its threshold then the United Kingdom's figure for 1982 and 1983 would have been as shown (safety net figures in brackets):

	Million ecu	
	1982	1983
Unadjusted Net Contribution	2036	1912
Adjusted Net Contribution	c.755 (437)	c.815 (525)
Reliefs	c.1280 (1599)	c.1100 (1388)

/(iii)

(iii) A French Proposal based on VAT Share/Expenditure Share Gap

3. The French Presidency have also been canvassing a mechanism based on the VAT share/expenditure share gap. The chief features of it are:

(a) The gap would be measured by the difference between VAT share and expenditure share operating on the allocated budget as presently defined except that less than 50% of administrative expenditure would be included in the allocated budget (this reduces the measured gap for the United Kingdom by something over 100 mecu).

(b) The threshold would be similar to our safety net so that a member state below 90% of average Community prosperity would have a limit of 0 (ie would be entitled to recover 100% of any gap between the VAT share and expenditure) rising by 0.007% of GDP for each percentage point increase in relative prosperity. However a member state above 120% of relative prosperity would receive no abatement. The chief effect of this is that the Germans would not benefit.

(c) A member state whose measured gap exceeded its threshold would receive abatement according to a stepped formula based on relative prosperity. A member state whose prosperity was between:

90% and 100%	of the Community average	would recover	65%	of the excess
100% and 110%	"	"	55%	"
110% and 120%	"	"	45%	"

4. This has a number of unattractive featurs for the United Kingdom:

(a) The relief is low. On 1982 figures, applied to relative prosperity in a Community of 12, the United Kingdom would have received relief of about 700 mecu (safety net - 1599 mecu) leaving a net contribution of about 1300 mecu (safety net - 437 mecu).

(b) The marginal contribution to extra spending is high (45% in 1982).

(v) The marginal contribution would rise greatly (from 45% to 55%) and the rate of relief would fall correspondingly, if, for exchange rate or other reasons, the United Kingdom's relative prosperity rose above 110% of the Community average.

ANNEX III

FRENCH TEXT FOR EUROPEAN COUNCIL CONCLUSIONS

The European Council in Stuttgart recognised the need for greater budgetary discipline. In fact it is essential that management of EEC resources shall be based on the same strict rules as those governing the management of public finances in the member states. Expenditure must therefore be determined by the means available, not the ther way round.

To this end, the European Council adopts the following guidelines:

1. At the beginning of the budgetary procedure, the Council (ECOFIN) shall set itself a 'frame of reference', that is to say the maximum overall resources to be used in the following financial year.

The frame of reference shall be established in consultation with Parliament.

2. Within that frame of reference and preserving Parliament's margin for manoeuvre, the Council shall set itself two guidelines, one for expenditure as a whole, the other for agricultural expenditure. In order to take economic fluctuations into account, agricultural expenditure shall be calculated over a 3-year average.

The Council shall also provide for a contingency reserve to be used on decision by the Council.

On these bases, the Commission shall draw up the preliminary draft budget.

3. Every 4 months, the Council (ECOFIN) shall monitor trends in expenditure as a whole.

In the event of the framework adopted being exceeded or in danger of being exceeded, the Council (ECOFIN) shall take the necessary corrective measures.

UNITED KINGDOM AMENDMENTS TO FRENCH TEXT ON BUDGETARY DISCIPLINE

A. Amend second paragraph to read:

"To this end the European Council adopts the following guidelines, and instructs the Council (ECOFIN) to prepare detailed proposals for their embodiment in a legal form as part of the Community's budgetary procedures;"

B. Amend first sentence of paragraph 2 to read:

"...the other to do with agricultural expenditure. For the latter, the rate of increase should be markedly less than the increase in the own resources base over a period of years. To take account of conjunctural fluctuations, the agricultural guideline is calculated on a three year average. If in any year, for exceptional circumstances, agricultural expenditure has to exceed budgetary provision for that year consistent with the guideline calculated for that year, the excess shall be recovered over the two succeeding years". and delete the second and third sentences of that paragraph.