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Foreign and Commonwealth Office

London SW1A 2AH

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New York

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Visit of M. Thorn: 17 March

All the subjects which M. Thorn is likely to raise over dinner at No 10 on 17 March are covered by the briefing which has already been supplied for the European Council and which will be discussed at the Prime Minister's meeting tomorrow afternoon. On the budget, however, she may wish to take a rather different line at this private meeting with M. Thorn. I enclose a brief for that purpose, prepared in consultation with the Departments concerned.

I am sending copies of this letter (without the enclosure) to John Kerr (Treasury), Robert Lawson (MAFF), Sir K Couzens (Department of Energy) and R Gray (Department of Trade).

John Kerr

R B Bone

(R B Bone)
Private Secretary

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VISIT OF M THORN: 17 MARCH 1983

EC BUDGET

Objectives

1. To ensure that President Thorn agrees to introduce separate discussions at the March European Council on the Green Paper and the solution for 1983 and later.
2. To persuade him to accept an obligation to make proposals on both to Foreign Ministers before the April Foreign Affairs Council.
3. To get his thinking on the nature of the solution for 1983 and later as close as possible to that of the United Kingdom.

Points to Make

4. Must get serious negotiation started as rapidly as possible on Community finances. You said to me last September that long negotiations do not always produce better agreements. 30 May Mandate discussion went on too long and fizzled out. We now have a narrow window between major elections in the Community and we must make the most of our chance.

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5. Problem has two aspects - reform of the financial system and an interim solution while that is being agreed and implemented. Both are extremely important. You should not think that, because we are calling for an interim solution, we are not interested in achieving a lasting reform. On the contrary, we want a reform of the system very badly, and always have done. We must get away from these repeated haggles. But we need also to deal with the immediate problem for Britain.

6. First step is a structured and serious discussion at next week's European Council of both aspects. Glad that you have agreed to introduce each item.

7. European Council should set clear timetable. We have been drifting, ever since November deadline for a settlement was missed. Now it is March, and we cannot go on waiting much longer. The Commission has produced discussion papers, but time has now come for you to make your proposals.

8. Hope therefore that you will agree to accept remit from European Council to produce proposals on both aspects in good time before April Foreign Affairs Council. If we are to stand any chance of getting

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agreement by June - and you know how important that is politically - then we need a serious discussion at the April Council and decisive progress at the May one. Clear that April Council will not get down to business unless Commission proposals have already appeared and been digested in capitals.

9. [If Thorn says that it cannot be done].

If Foreign Ministers do not start work in April, only chance of agreement before June lies in their May Council. Surely you cannot expect them to reach agreement in only one meeting? I do not need to explain to you how sensitive the budget issue is in the UK debate about Community membership and how crucial politically it will be to have an agreement by June; I know from Sir Robert Armstrong that you understand that and will do your best to help get such an agreement. But is there any other realistic way of doing so than what I have suggested?

10. Own Resources. I mentioned in my letter to you how important it is to ensure that we make most effective use of resources we have. The Community is not doing so now. Tugendhat has warned of alarming trends of rising CAP expenditure. That must be brought

under control. Under present arrangements new money would be likely to be used to finance disposal of even more surpluses, and to make British burden heavier, not lighter. And the present own resources are rising by 8-10% a year.

11. Green Paper. Identifies some ideas which could be developed into a solution to problem of imbalances:-

a) new policies can make a contribution to solving the problem, but as you recognise only a small and gradual one. (Improving balance of spending policies desirable in its own right).

b) tax based on agriculture indicators could also help, but I am sure it could only be at best a partial solution to the problem.

c) Financial equalisation system no help if just a way of helping least prosperous, but is that Commission's intention? Such a system could be designed as a safety net to correct the imbalances. Would need however to have an equitable way of measuring imbalances.

12. Discussion at the Foreign Affairs Council showed that several other Member States had difficulties with the agricultural tax. Would it not be simpler to take

up Chancellor of the Exchequer's recent suggestion and
reduce VAT liability of any member state bearing an
excessive budget burden? Our feeling is that this
could be more negotiable. The idea would provide
safety net, which would be effective for as long as
budget arrangements produced an inequitable result.
The safety net could be determined by such factors as a
country's GDP and relative prosperity. Reducing VAT
rates would remove need for CAP related source of
revenue and remove current political problems over
special expenditure for Britain and Germany. Our
impression is that the French and Germans are not
entirely unsympathetic to this idea.

13. Solution for 1983 and later.

We agree with the suggestion in the November paper that
the solution should be on similar lines to those for
1980-1982. There would then be three components: the
basic refund; the risk-sharing arrangement; and the
duration.

(i) Basic Refund. The refunds would have to be
calculated as a percentage of the Commission's
estimate of the United Kingdom's unadjusted net
contribution in each year, with a risk-sharing
formula upwards and downwards. The key question

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Community does indeed pose a problem. Now that their election is over, they must be persuaded to change their view. I hope that you will take the matter up with Chancellor Kohl personally.

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(ii) Risk-sharing. The risk-sharing formula for 1982 was regarded in London as very unsatisfactory and would not have been agreed but for the Falklands war and the unexpectedly good results for the United Kingdom in 1980 and 1981. We must now go back to the formulae in the 30th May 1980 agreement.

(iii) Duration. I have said that the solution ought to last as long as the problem: I hope that the Commission would undertake to propose that the system agreed for 1983 and 1984 be extended if the reform of the financial system agreed as a result of the Green paper proposals were not in place by 1985.

14. Overpayments. The Commission have acknowledged that the 1980 agreement was carried out strictly in accordance with its terms. There is therefore no legal obligation on the United Kingdom to make any restitution. But we acknowledge the political case and

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is what basic percentage would be fair to both sides (leaving aside for the moment the alleged over payments). The 30 May Agreement was constructed on a 66% refund. The out-turn was higher and the arrangement has been criticised for that reason. The percentage for the top slice of the risk-sharing formulae was 75%. There is, therefore, no reason to expect other member states to agree to a higher percentage than 75%. Equally, there is no reason for the United Kingdom to accept a lower percentage than 66%. We would expect the negotiations to take place within that bracket.

[If Thorn then says that 66% would be too high.]

Then I must warn you that there is no chance of an agreement. Given what the Community accepted as fair in 1980, and given the results of the 30 May Agreement, we would regard it as extremely provocative if the Commission were to propose a basic percentage (ie ignoring over-payments) which was lower than 66%.

[If Thorn protests that this is not achievable, particularly in light of the German position.]

The current German insistence that they will only pay 25% of their normal contribution to the



have already conceded around 200 mecu in the agreement for 1982 after risk-sharing has been taken into account. The "overpayment problem" must be dealt with at the same time as the solution for 1983 and later because the United Kingdom's attitude will be determined by the attitude of other member states to the solution of the underlying problem.

15. [Defensive - Withholding.] I have told the House of Commons on 27 January that I hope that a lasting solution for 1983 onwards will be found by negotiation so that there will be no question of withholding . But for political reasons the need to find a solution soon is increasingly urgent. The United Kingdom is moving towards an election in which membership of the Community is an issue; the Opposition will fight for withdrawal. It would be almost impossible for the government to win the argument if Labour could say that we had to pay so much in 1983.