

Ref. A01725

PRIME MINISTER

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Community Budget

I have been trying to take stock of the negotiating prospects and possibilities on this subject. This note tries to sum that up. I am afraid you will think it wet, and I have been on the point of not putting it in on that account. But I think I should: it is not addressed to the question what would be the best outcome from our domestic political or financial point of view, but to the question what we are in reality likely to be able to negotiate with our partners. That is a matter on which you and your colleagues will need an assessment and should form a view. You may decide that the lowest figure we require is higher than the largest figure we can get, and accept the consequences of that decision; but at least that should be a decision which you take consciously, not by accident or because of our failure to tell you what we think the negotiating prospects are.

2. The figures in this note are all in terms of net rebate: what we can get back. I think the discussion in Dublin is bound to be in those terms. If we can agree with our partners on a net rebate, we must then try to convert that into a net contribution and get a commitment for the future expressed in terms of that. I come back to that in paragraph 10 below.

3. As you know, thanks to the virtual disappearance of MCAs and other factors, we are now thinking in terms of a net contribution in 1980 of about 1,700 meua (£1,135 million). That is in line with the "exporter benefits" figure we were talking about in December, but of course higher than the 1,550 meua figure on an "importer benefits" basis which you used for your presentation at Dublin.

4. You indicated to Signor Cossiga in January that we were ready to come down by (i.e. agree to a net contribution of) 200-250 meua. Starting at 1,700 meua, that brings our present bid to 1,450 meua (£965 million); starting from 1,550 meua - the figure we had in our minds at that time - it would bring the bid down to 1,300 meua.

5. There is in my judgment no prospect of agreement from our partners on a figure of 1,450 meua, either this month or in June. This is not just a matter of French intransigence, which we might hope to isolate. Our paying 1,450 meua less would mean our partners providing 1,450 meua more. Other Community countries are struggling with public expenditure problems no less serious for them than ours is for us: Belgium is a particular case in point, but not the only one. The Germans have special problems. In a year with an election at the end of it, they have in the last few months accepted considerable new commitments for aid to Turkey and aid to Pakistan (and we shall no doubt want them to join in with us in providing aid to Zimbabwe). They have problems not only of public expenditure and high (for them) interest rates; and they are now in balance of payments deficit for the first time for 25 years.

6. Understanding of our position and needs has grown considerably among the partners since Dublin. The "methodology" of a settlement is now generally accepted. People are talking about higher figures than they were talking about at the time of Dublin. But the other difficulties of other Governments are if anything growing rather than diminishing. Some issues - e.g. fish - will be more difficult in June than they are at present. I do not suggest that we have anything to lose - in terms of negotiating prospects on the budget contribution - if we have to wait until June. But I do not think that the outcome would be significantly better if we waited until June, and therefore I doubt whether there is any reason not to try hard for a settlement this month.

7. How has negotiation on the figures gone, and how might it go from here? What follows assumes that they start from wanting no change in our net contribution (0 meua) and we start from wanting broad balance (1,700 meua):

(i) At Dublin they initially conceded 520 meua on the revised financial mechanism. We shall get about half of that anyway on the mechanism as it is.

(ii) When Cossiga came we conceded 250 meua.

Score so far: 520/1,450.

(iii) The Dutch and others have talked in terms of 800 meua in all - a move upwards of about 300 meua.

(iv) If that sort of figure is in the air in Brussels, they will be looking to us for corresponding signs of progress. Should we be prepared to move by about half of their move - say, by 150 meua to 1,300 meua (which is, in a sense, the figure we thought we had moved to with Signor Cossiga in January)? If so, score so far: 800/1,300.

8. This suggests that the area in which an eventual settlement might emerge is between 1,000 meua (the figure canvassed by Roy Jenkins, equivalent to £665 million) and 1,200 meua (£800 million). If we could get the figure up to 1,135 meua, that would imply their giving 2 meua for every 1 meua given by us. It would be equivalent to a cut of £760 million, or two-thirds, in our net budget contribution, leaving it at 565 meua (£375 million). But this looks to me to be at the extreme outside edge of what the partners are likely to concede, and perhaps even beyond it (one German official has said in terms that a two-thirds/one-third compromise would not be acceptable to the Germans, though that does not have to be the last word. On the other hand a figure of 1,000 meua (about £665 million), which we would stand a better chance of getting, would leave us still to find 700 meua (about £465 million). That seems to me to be the very lowest limit which we could conceivably accept (at £665 million, it is in fact a little better than the £600 million mentioned in Peter Jenkins's article in The Guardian).

9. It is possible that the Brussels Council in March could agree on a total figure, and instruct the Commission to put to the Council of Ministers proposals for achieving that figure in 1980, if for our part we were able to indicate readiness to accept an arrangement for sheepmeat, and willingness to contemplate a CAP price settlement which included some increase in prices. That would not in fact be final, because the French could be difficult about the detail of the proposals on the budget contribution and we could be difficult about the detailed implementation of flexibility on CAP prices. But we should have won agreement on a figure for the reduction of our net contribution.

10. Duration is important to us; and there will be some trade-off between duration and the figure. We want a settlement that puts the problem away at least until after the next election here. We probably cannot get agreement to an auto-

matic receipts mechanism. What we might be able to achieve would be an agreement that the Commission should be instructed to make proposals as and when necessary to ensure that in 1981 and subsequent years our receipts, as a percentage of average receipts from the budget, are no less than that resulting from the figure agreed for 1980. Or we could go for a formula expressed in terms of our net contribution: that in 1981 and subsequent years it should be no greater in proportion to the total budget than the agreed figure for 1980. Whatever the formula, we shall want it to apply at least until 1984 and preferably until 1985.

11. We must also seek the strongest formula we can get on restructuring, on the lines put to Signor Cossiga. It will be important to us in future discussions, even if we see no chance of early and positive change.

12. As to what we do if there is something like a breakdown in negotiations in Brussels, our partners are increasingly aware that the possibility of withholding part of our contribution is in our minds. I understand that the Leader of the Opposition recently asked what would be the German reaction to our withholding the VAT part of our contribution. He was told that that would precipitate a deep and serious crisis. My own judgment is that actually to withhold any part of the contribution would be more likely to harden the attitudes of our partners than to lead them to agree to a larger reduction in our net contribution. That suggests that, if we actually withheld, we should be in a very real danger of finding ourselves on a slippery slope that led irrevocably to withdrawal of virtual exclusion. But that does not preclude, if we do not get a settlement at the March Council and have to wait till June, talking about the possibility of withholding, in very much the terms you have been using, of sorrowful reluctance rather than angry threat: we are very reluctant to contemplate any step that would involve a breach of the law or of our Treaty obligations, but our problem is such that we cannot absolutely rule out the possibility, if we cannot manage to reach agreement as we hope and are trying to do.

13. I suggest that, if we do not get a settlement at Brussels, we shall need to continue to stick strictly to our position on sheepmeat; to be intransigent on CAP prices; not to offer any statement on energy; and to continue to make slow progress

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towards a Common Fisheries Policy. On EMS, any concession we might make this month cannot go beyond some commitment in principle to join when the conditions are right. There is no likelihood of the conditions for our entry being met between now and June. So, if Ministers are minded to make any concession - on which I am submitting a separate note - I think that it could be safely made in March, and would be a useful demonstration to the Community of the Government's commitment to the Community and a counterbalance to what will be seen as our intransigence on other matters, including the CAP prices and our budget contribution.

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ROBERT ARMSTRONG

18th March, 1980

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