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Treasury Chambers, Parliament Street, SW1P 3AG
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20 February 1984

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See John,

EUROPEAN COMMUNITY EXPENDITURE AND THE CONTROL OF UK
PUBLIC EXPENDITURE

The Chancellor and the Secretary of State for Trade and Industry have discussed in some detail the options set out in E(A) (84)12, and as a result wish to table, before tomorrow's ... E(A) discussion, the joint proposal set out in the attached memorandum.

I am accordingly sending copies of this letter and the memorandum to the Private Secretaries of all members of E(A), the Foreign Secretary and the Secretary of State for Education and Science; as well as to Sir Robert Armstrong, Dr Nicholson and David Williamson in the Cabinet Office.

*Yours ever,
John Kerr.*

J O KERR

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EUROPEAN COMMUNITY EXPENDITURE AND THE CONTROL
OF UK PUBLIC EXPENDITURE

Memorandum by the Chancellor of the Exchequer and the Secretary
of State for Trade and Industry

We are to discuss the question of European Community expenditure and the control of UK public expenditure at E(A) on Tuesday.

2. There is general agreement that we should set up a new PESC Sub-Committee. This will be a useful instrument for improving our forecasting of Community expenditure and more importantly, determining our priorities within it.

3. The note by the Chairman of EQS (E(A) (84)12) usefully sets out three possible options for bringing new Community expenditure programmes properly within the ambit of our public expenditure control procedures and for avoiding additionality. It is highly desirable that we should settle the questions raised in his note quickly in advance of the 1984 PES round. We also need to take urgent decisions on our approach to ESPRIT before the 28 February Research Council.

(a) PES Procedures for EC Expenditure

4. Paragraphs 9 and 10 of E(A) (84)12 describe the agreed existing arrangements for non-additionality and attribution which have governed the traditional areas of Community expenditure since our accession in 1973.

5. As we agreed at E(A) (83)8th meeting, we need to complement these arrangements with effective mechanisms for ensuring that UK public expenditure is not increased by the proliferation of new



spending programmes, already totalling some billions of ecus, which have been tabled by the Commission in recent months. There are three requirements which any effective mechanism has to meet. It must provide:

- a strong incentive to hold down the cost of Community programmes;
- a procedure for assessing the priority of new Community expenditure proposals in comparison with each other and with domestic public expenditure programmes;
- a means of ensuring that our agreed domestic public expenditure programme totals are not exceeded by the addition of receipts from the Community Budget.

6. We have examined the Cabinet Office's Option 3 with these criteria in mind. After discussion we believe that - with some modifications - it can provide the basis for a satisfactory system, which will ensure that these new Community expenditures are subjected to proper scrutiny as part of our normal PES arrangements, but with a degree of flexibility to take account of the Community dimension.

7. The note at Annex A sets out our agreed proposals for a new system modelled on Option 3. The main points in it are:-

- a mini-Euro programme will be established for R & D, industrial and infrastructure support expenditures. The UK's priorities and negotiating aims on these programmes will be discussed early in the year as part of the PES process;
- within the new programme UK spending Departments



will act as the sponsors for the UK financing share of the Community expenditures which fall in their functional areas. But there will be opportunity for offsetting increases in Community expenditure on one part of the programme against genuine savings elsewhere within the programme;

- subject to what is said below on ESPRIT the baseline for the mini-Euro programme will be calculated from the provision for the relevant expenditures in the 1984 Community Budget. This baseline will subsequently be updated each year in line with the general rate of increase in UK public expenditure;
- any proposals for increases going beyond the baseline will be the subject of scrutiny under the normal PES procedures. Where Cabinet agrees that some increase in Community expenditure on these programmes is inescapable, but that offsetting savings cannot reasonably be found by the sponsor Department, the increases will be offset across public expenditure programmes as a whole;
- in the case of multi-annual Community spending programmes which are subject to a fixed ceiling any underspending in one year can be carried forward and added to the baseline in the later years, provided the total size of the programme remains the same. Where expenditure on an agreed multi-annual programme runs above the profile in a particular year, offsetting savings within the year would not be required, but corresponding reductions would be made in the baseline in the later years of the programme.



8. So far as ESPRIT is concerned we are now agreed that we should seek to ensure that it is given special priority within the funds available within the Community Budget. Paragraph 10 and Annex B below set out the line we believe we should now take at the 28 February Research Council. In these circumstances it is considered reasonable that ESPRIT should be accorded the same priority within the new PES control programme. A special addition will accordingly be made to the EURO-PES baseline to cover our full contribution to ESPRIT throughout the PES period.

9. We believe that, if E(A) can endorse these proposals, they will provide a satisfactory framework for deciding on our priorities among Community expenditure programmes and controlling the consequences for our own public expenditure totals.

(b) ESPRIT

10. On ESPRIT itself, the next step must, we believe, be to build on the German proposal made at the last Foreign Affairs Council - that the money for ESPRIT must be financed from within an overall "financial envelope" for payment credits on Community R & D of 600 mecu a year at least for the next two years. In order to establish the implications of this the Commission must now be pressed hard to bring forward their estimates both of the payments needed to meet R & D commitments already entered into in 1984 and 1985 and of the amounts left available within the 600 mecu figure for new expenditures. We will need convincing assurances that the lower priority R & D programmes will be scaled down in size in order to make room for ESPRIT and other high priority commitments such as the Joint Research Centre. Annex B sets out in more detail the form we believe these assurances should take. Provided we can get satisfactory answers from the Commission, we should be in a position to agree to the ESPRIT programme going ahead, preferably at a level of 700 mecu, but, in the last resort at 750 mecu.

NL
HM Treasury

NT
DTI

20 February 1984

EC EXPENDITURE PROGRAMMES AND
UK PUBLIC EXPENDITURE CONTROLS

(a) THE "FORWARD LOOK"

(1) A Sub-Committee of PESC (PESC(EC)) will be set up to carry out the "Forward Look" at Community expenditure, as proposed in paragraphs 4-8 of E(A)(84)12. Its tasks will include, as part of the "Forward Look", the collective discussion of, and where possible agreement on, the UK's priorities across all Community expenditure programmes for use in substantive discussions in Brussels. In addition, PESC(EC) would also be the forum for discussion of any questions on the proposed new PES control procedures set out in paragraphs 2-11 below.

(b) PESC TREATMENT OF COMMUNITY EXPENDITURE

(2) The existing arrangements for non-additionality and attribution set out in paragraph 9 of E(A)(84)12 will continue to apply. The arrangements for the non-quota section of the ERDF are discussed in paragraph 12 below.

(3) A separate mini-EURO-PESC programme would be established as an internal control total for the UK's financing share in all new Community expenditure on R & D, and industrial and infrastructure support, as proposed in Cabinet Office Option 3. Within this programme each spending Department will follow the procedures set out below for the UK financing share of any Community spending proposals for which it had functional responsibility.

(c) CALCULATION AND UPDATING OF BASELINE

(4) The 1984-85 baseline figure for the mini-EURO programme should be based on the level of payments appropriations in the 1984 Community Budget. For later years the 1984/85 baseline would be increased in line with the general rate of increase in total UK planned public expenditure. A special supplementary addition to the baseline will also be made throughout the PES^{period} to cover the full costs of the ESPRIT programme to the extent that these exceed the provision for ESPRIT in the baseline.

(5) The UK public expenditure consequences of any increase in Community expenditure above the baseline will be measured in terms of the UK financing share of the Community expenditure in question (currently 22%) less those public sector receipts which are required to be surrendered to the Consolidated Fund under the European Communities Act

(6) There will need to be safeguards to prevent individual projects receiving like support from a Community and a domestic programme. (ERDF trigger expenditure apart).

(7) Where the Community agrees a multi-annual commitments programme, the best possible forecast of the payments profile would be made in order to assess whether it could be contained within the baseline. The forecast will however be uncertain. In order to deal with that uncertainty there should be provision, where Community expenditure on a multi-annual programme falls below the expected profile provided for within the baseline, for any underspend to be carried forward and added to the baseline for the next year. Where expenditure on an agreed multi-annual programme runs above the profile in a particular year, offsetting savings within the year (see paragraph 10 below) would not be required, but corresponding reductions would be made in the baseline over the later years of the programme.

(d) OPERATION OF THE PROGRAMME IN THE PE SURVEY

(8) As early as possible in each year's PE Survey PESC(EC) would establish agreed baseline figures for the programme for the years covered by the PES Survey in accordance with the ground rules above and would collectively seek to agree on the UK's priorities within the baseline as a guide to determining the UK line in Brussels.

(9) Where Community expenditure was expected to rise above the baseline level, the UK public expenditure consequences of this excess would be put forward by the sponsor Department as an "additional bid" within the normal rules of the PE Survey. Where it is proposed that such an additional bid should be accepted within the agreed totals for public expenditure, offsetting savings would need to be made as follows:

(a) offsetting savings would be sought from elsewhere within the total available for the mini-Euro programme to the extent that genuine and continuing reductions in other elements within the baseline could be identified with certainty. The scope for and use of such offsetting savings would need to be determined collectively in PESC(EC).

(b) where no savings within the Euro-programme were available, the domestic expenditure programmes of the sponsor Department (where there is one) would be scrutinised for offsetting savings as part of the normal PES procedures.

(c) when as a result of the PES scrutiny it is proposed to Cabinet that the offsetting savings cannot fully be made from within the Departmental programme, any excess would have to be found by savings within the public expenditure programme.

(e) CONTROL OF THE PROGRAMME DURING THE YEAR

(10) Where the level of Community expenditure increased during the year (eg as a result of new decisions or a Supplementary Budget) beyond the level allowed for in the PES, offsetting savings would be looked for within the total available for the mini-Euro programme. Where no savings within the Euro-programme are available, the domestic expenditure programmes of the sponsor Departments would be scrutinised for offsetting savings.

Where such savings cannot be made, access to the Reserve would be considered in accordance with normal rules. Any continuing increase in later years would have to be put forward as an additional bid in the next year's Survey.

(f) SAFETY NET

(11) This mechanism will need to be reviewed once the corrective budgetary mechanism within the Community has been established.

(g) ERDF NON-QUOTA SECTION

(12) The non-quota section of the ERDF would, as at present, be subject to the non-additionality rule. Receipts going to the private sector would be disregarded. The "trigger payments" which the Government will have to make to enable the private sector to claim these receipts will continue to be financed on the DTI's programme. The PES treatment of these trigger payments will be reviewed when any new non-quota section programmes for the UK are proposed.

ESPRIT

1. The UK should be prepared to agree to the launching of the ESPRIT programme only if there is also agreement on ^{an} annual total payments ceiling for all Community R & D programmes and on the necessary decisions to cut back commitments on other R & D programmes (see 3 below). The Germans have proposed that this payments ceiling should be fixed at 600 mecus. We should support this figure, but in the last resort be prepared to move to 670 mecu (which is the maximum available within Chapter 70-73 of the 1984 Budget, including some provision within Chapter 100).
2. Within the agreed payments ceiling priority would be given, as proposed by Germany, to ESPRIT, the agreed JRC programme and fusion programme. Expenditure on other R & D programmes would have to be contained within what was left.
3. To ensure that the payments ceiling is observed the size of the Community's other multi-annual R & D programmes may have to be cut back or deferred. Specifically the Commission would have to undertake to hold down commitments on other R & D programmes in 1984 and 1985 to a level which ensured that the 600-670 mecu payments ceiling was respected. The level of the R & D payments ceiling for 1986 and onwards could be reviewed before the end of 1985.
4. No decision to go ahead with the ESPRIT programme until the Commission had produced forward profiles for expenditure on ESPRIT and the other R & D programme for at least 1984 and 1985 showing that they could be accommodated within the 600-670 mecu payments ceiling in those years.

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20 JAN 1984



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Mr AJ Coles

Ref. No: EA (84)3

Date: 20.2.84

Notes in connection with a motion
in the House of Commons on

Monday 20th February 1984

to take note of the European Community
documents on the Draft General Budget
for 1984

Conservative Research Department,
32 Smith Square,
London SW1
Tel. 222 9000

Enquiries on this brief to:
Peter Cropper

Five items are before the House:

- 1) The Preliminary Draft Budget of the European Communities for 1984. (Presented 10th June 1983).
- 2) The Draft budget of the European Communities for 1984.
- 3) The European Parliament's modifications and amendments to the Draft General Budget of the European Communities for 1984.
- 4) The Annual Report of the European Court of Auditors for the financial year 1982.
- 5) Sixth Report from the House of Commons Select Committee on European Legislation.

The Draft General Budget for 1984 consisted of seven volumes, including individual budgets relating to the Community institutions. The Budgets of the Council, the European Parliament, the Court of Justice and the Court of Auditors are almost entirely for their administrative and running expenses. The main Community policies (e.g. the Common Agricultural Policy, the Social Fund, Regional Development Fund, Aid etc) are financed out of the Commission's budget, which accounts for some 98% of the expenditure in the Draft Budget as amended and modified by the Parliament.

The Parliament considered the draft Budget as decided by the Council of Ministers on 20-22 July 1983, and made various proposals for increased expenditure. These proposals were in turn amended by the Council; the Budget was declared adopted on 20 December 1983. The principal proposals were:

	<u>Parliament's proposals</u>		<u>Council's decisions</u>	
	Payments	Commitments	Payments	Commitments
Social Fund	£74m	£136m	£74m	£68m
Regional Development Fund	£69m	£216m	£69m	£62m
Aid	£72m	£132m	£43m	£56m
Energy	£50m	£69m	£30m	£34m
Research and Investment	£18.5m	£129m	£3m	£46m
Transport	£1m	£28m	£0.7m	£10m

European Court of Auditors for 1982 represents, in the view of the British Government, an important step in the development of financial control within the European Communities.

Sixth Report for the House of Commons Select Committee (23 November 1983)
considered problems of the future financing of the European Community viz:

- i) Various proposals to increase the revenue of the Community;
- ii) a fairer sharing of the burden of funding Community expenditure;
- iii) control of CAP expenditure.

The Select Committee noted the British Government's position, that the United Kingdom would be prepared to consider an increase in own resources provided:

'First, that agreement was reached on an effective control of the rate of increase of agricultural and other expenditure; and secondly, that it was accompanied by an arrangement to ensure a fair sharing of the financial burden' (Sir Geoffrey Howe, Hansard, 14th November 1983, Col. 611).