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*From the Private Secretary*

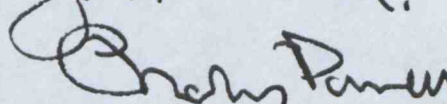
13 February 1990

Dear John,

EMU

Thank you for your letter of 12 February describing the point reached in the monetary discussions of EMU and setting out the line which our representatives intend to take in discussion on budgetary policy next week. I have shown this to the Prime Minister who is content with the four stipulations we might propose for an amended treaty.

I am copying this letter to Stephen Wall (Foreign and Commonwealth Office) and Sonia Phippard (Cabinet Office).

Yours sincerely,  
  
Charles Powell

John Gieve Esq  
HM Treasury.

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cc/c  
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Treasury Chambers, Parliament Street, SW1P 3AG  
01-270 3000

12 February 1990

Charles Powell Esq  
Private Secretary to the  
Prime Minister  
10 Downing Street  
LONDON  
SW1A 2AA

*Ric Lewis*

Dear Charles

*I think there  
four points are  
all revised.  
nt*

*Agree the  
line which it is  
proposed to take?*

*CD 13/2*

**EMU**

The European Council agreed at Strasbourg that the General Affairs Council and the ECOFIN Council should use the period prior to the opening of an Inter-Governmental Conference on EMU, before the end of 1990, to ensure the best possible preparations. It is very much in our interest that as much of this preparatory work as possible is carried out under the auspices of ECOFIN so as to ensure that the technical problems of a move towards EMU are fully recognised. To that end, the Monetary Committee, composed of senior officials from Treasuries and Central Banks, have begun to review what might be involved. The Committee plan to produce a report which ECOFIN would consider, probably at its informal meeting at the end of March. The Chancellor will, of course, discuss his line with the Prime Minister for that meeting, in the light, among other things of the work being carried out by an interdepartmental group of officials which was foreshadowed in my letter to you of 30 November.

In the meantime officials are doing the best to ensure that the Monetary Committee's report is as helpful as possible. While they serve on the Committee in their personal capacities so that their views do not commit the UK, the Prime Minister may wish to be aware of the line that they have in mind to take in the





discussion on budgetary policy next week. As you will recall the Delors Report argued that there should be binding budgetary rules on Member States. There is some support for this in the Committee but also some backing for the UK's view that such rules are neither necessary nor desirable. Our representatives intend to argue that, if there is to be an amending treaty, it could include requirements:

- (i) to prevent monetary financing of budgetary deficits;
- (ii) to prevent bail-outs of Member States by the Community Budget or other Member States;
- (iii) to impose in the context of Community mechanisms for lending to a Member State (if these mechanisms continue), a legally binding budgetary commitment upon that Member State as a condition of the loan. But there would be no such commitment unless the Member State voluntarily accepted the need for a loan and the accompanying conditions;
- (iv) to establish, in order to underline the undesirability of excessive budget deficits, binding procedures on Member States for the conduct of economic surveillance, including national budgetary policies, within the Community. The crucial element here is that what would be binding would be the procedure for the surveillance exercise, not its outcome eg in the form of Delors' binding budgetary rules. The procedure might, for example, cover the circumstances in which a special examination of a country's budgetary policy could be initiated, the scope of such an examination, and the roles of the Commission, the Monetary Committee and ECOFIN.

3. The first two stipulations were referred to in the UK's paper, "An Evolutionary Approach to Economic and Monetary Union". The third would in effect incorporate into the Community legal framework the conditionality associated with an IMF loan. But that conditionality could only bind Member States if they voluntarily accepted the need for a loan and the accompanying conditions. The Chancellor thinks that the fourth stipulation above is acceptable provided we are clear that the binding element applies only to the procedure. Such a procedure could provide a useful buttress to the process of multilateral surveillance within the Community, which is an important element in the UK's evolutionary approach.

4. An approach on the lines described above should find some support in the Monetary Committee and it would be most helpful in ECOFIN if it were reflected in their report. But the Chancellor thinks that even if it does not, the approach is clearly the right one and we should continue to press it.

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5. I am sending a copy of this letter to Stephen Wall in the FCO and to Sonia Phippard in the Cabinet Office.

V. J.

J.G.

**JOHN GIEVE**  
Principal Private Secretary