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CABINET**EUROPEAN FREE TRADE AREA****MEMORANDUM BY THE PAYMASTER-GENERAL**

The negotiations on the establishment of a European Free Trade Area have reached a crucial stage, and I need the advice and guidance of my colleagues.

2. The 17-nation Committee have been working on the basis of a comprehensive agenda, every item on which has been discussed. The positions held by all the countries are now clear.

3. The time factor is important. Our object is to ensure that the tariff reductions in the Free Trade Area coincide with those under the Treaty of Rome, which begin on 1st January, 1959. To do this we must ensure that we have reached substantial agreement before the summer holidays. In any case, failure to reach agreement by then is likely to mean that public support for the whole project will grow cold. There are, it is true, many points of difficulty. But the fact is that no country has been prepared to embark upon a real negotiation on details while the question is still open whether there can be any basic agreement at all. Once it has been established that the major Powers can agree on the major issues, then people will begin to negotiate and rapid progress can be made.

4. The three major issues remain as they have been throughout—agriculture, what is known as the question of origin, and the problem of France. I dealt with these points in my paper (C. (58) 27) which was discussed by the Cabinet on 4th February (C.C. (58) 14th Conclusions, Minute 6). Developments since then have been as follows.

Agriculture

5. There is little more to report on this score. The difficulty has been that while other people have been prepared to criticise our ideas, they have not produced counter-proposals. There are now signs that they are beginning to do this. At the next meeting in Paris on 31st March I hope to have papers available from several members of the Committee, including, I hope, an agreed paper from the "Six"—France, Germany, Italy and the Benelux countries. I shall be in Copenhagen on 20th and 21st March and I hope next week to be able to give my colleagues orally the latest news about agriculture.

Origin

6. We had a useful discussion on this subject in Paris last week. Two facts in particular were established:—

- (i) that there is no support for the French attempt to use the rules of origin to protect themselves against competition from products produced entirely within the Free Trade Area;
- (ii) that no serious practical problems can arise from the absence of a harmonised external tariff for at least four years from the start of the Free Trade Area.

Subject to this the fact remains that there is still a great division of opinion between two schools of thought. The first, comprising France, Italy and to some extent

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Belgium, wishes to maintain a high tariff structure on a wide range of raw materials and semi-manufactures and therefore considers it necessary to have strict origin rules defined in advance. The remaining members of the Committee do not believe in a high tariff policy of this kind, but consider that the practical problems likely to arise will not be great and cannot be defined beforehand and that what is needed is some simple institutional provision for dealing with any problems as and when they do emerge. The Italian representative, Professor Carli, produced a new plan as an attempt at a compromise. The plan as it stands would be quite unacceptable to both sides, but expert study is being given to it and there is just a possibility that if drastically altered it might make some contribution to solving the problem.

France

7. The French attitude remains as hostile as ever. Based as it is on a combination of deep-seated protectionism and violent jealousy of Britain, and fanned by the vigorous propaganda activities of the French employers, it presents a formidable obstacle to agreement. The French have produced a plan which they have put to their colleagues in the Six; as it stands it is acceptable to none of them, but urgent attempts are being made to produce a revised plan. The aim is that this plan should be approved by the Ministers of the Six at a meeting on 22nd April and then transmitted to the Paris Committee for immediate consideration by the "Seventeen."

The British Position

8. We entered these discussions with very limited room for negotiation. We are not prepared to give any commitments of a specific character on agriculture; we have declared our intention of maintaining our special relations with the Commonwealth; we are not prepared to accept any of the provisions for harmonisation of industrial, social and commercial policy that are an essential feature of the Treaty of Rome. The Free Trade Area proposal is in fact tailor-made to suit British requirements.

9. We have been able to make minor concessions on one or two points. For example, we have agreed that agriculture should be discussed, though not on the same basis as industry. The Commonwealth countries will lose such preferences as they enjoy, compared with Europe, in industrial products. We have recognised that a Free Trade Area will mean closer co-operation between member countries in economic and financial policy and will involve an implicit obligation in each country not to use its commercial freedom so as to damage its neighbour or, at any rate, if damage proves inevitable, to provide some compensation. So far we have been able to retain the general impression that the British are being reasonable and accommodating and genuinely seeking agreement. It is we who have been holding the initiative, and it is the French, with occasional support from the Italians and other members of the Six, who have been the negative factor. Our objects in the crucial phase that is approaching must be:—

- (a) to achieve success at some acceptable cost;
- (b) if the cost proves unacceptable, not to give the impression that it is our intransigence that has caused the breakdown.

We must not under-estimate the blow to the whole of Europe that would follow a breakdown in the negotiations now they have progressed so long and so far. Courtship so prolonged has reached a stage where a break between the partners would leave a deep and bitter scar.

10. It is possible to classify our allies and our opponents on roughly the following lines:—

Our Allies

(i) *The Scandinavians*

Denmark has a problem with agriculture and Norway with fish. But, in general, the UNISCAN solidarity is being well maintained.

(ii) *The Swiss*, who possess the two great assets of a trade deficit with the Six and an extremely strong currency.

(iii) *Austria*

- (iv) *The Benelux countries.*—They support us by reason of sentimental attachment, because as small countries they feel rather lost and alone in the Common Market with Germany, Italy and France, and because of their low tariff traditions.

(There is developing a very interesting connection between the countries mentioned in (i) to (iv) above. It is a kind of small country, low tariff, Social Democrat network, which may be very useful, particularly as their ideas seem generally sympathetic to us.)

- (v) All those, in every country, who share the general political urge to European unity.
- (vi) Professor Erhard, and those other Members of the German Government who believe in Free Trade and low tariffs and who think they have already paid France too high a price for the Treaty of Rome.

Our Opponents

11. These are:—

- (i) *The protectionists everywhere.*—They are at their strongest and most powerful in France, but French protectionism strikes chords in Italy and in the Benelux countries, and there is some reason to suppose that a good deal of European protectionism is hiding under France's skirts.
- (ii) *The European Establishment.*—This consists of European senior officials and civil servants, men like Hallstein, Marjolin and Monnet, who exert an enormous influence. They regard the Common Market, the Coal and Steel Community and Euratom as their own triumph (as, indeed, they are). They fear that our ideas may disrupt this great new system and they are also inclined to say that the British, who were stand-offish at first, might just as well be left now to cool their heels in the lobby for a little while. The influence of this group of people is very considerable indeed and might become decisive if by reason, for example, of our apparent intransigence their Ministers should waver in the political support that they seem generally to give to the Free Trade Area.
- (iii) *The Francophil Germans,* led by Dr. Adenauer himself.
- (iv) *The French.*—Their hostility, based, as I have said, on the combination of protectionism and jealousy, is fanned by the propaganda of the employers and supported pretty well throughout French political life. The Free Trade Area proposal has no organised support whatsoever from any Party in the Assembly at the present moment. But the fact remains that the French, like all of us, have now a vested interest in the negotiations. A breakdown in the negotiations would mean not only a rupture with us but also a very severe strain indeed on their new-found friendship with Germany.

12. These seem to me to be the factors in the equation. Our bargaining position probably is weaker than the French because the mass is more immovable than the forces are irresistible.

Future Tactics

13. The question is how we should play the hand now. There are three possible results that may emerge from the consideration of the French plan by the Treaty of Rome countries:—

- (i) They might produce a plan which we could accept. This is, to say the least, extremely unlikely.
- (ii) They might fail to agree among themselves. Though superficially this might suit us, in the long run I fear it would be very dangerous because it would produce a disruption in Europe.
- (iii) They might agree on a solution that was unacceptable to us. This also would be very dangerous because by the very act of agreement among the Six they would have done much to freeze their negotiating position.

14. The main elements in the French plan to which we object are:—

- (i) the proposed industry-by-industry approach;
- (ii) the proposal that there should be prior harmonisation of many of the economic factors affecting competition;

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- (iii) the proposal that the Free Trade Area tariff reductions should start some years later than the reductions in the Treaty of Rome;
- (iv) the French desire to share in our Commonwealth preferences.

15. I think we can probably rely on the other Treaty of Rome countries to reject the industry-by-industry approach, which is quite impracticable and really is a disguised way of wrecking the negotiations. I think we can also rely on them to reduce the French proposals on harmonisation to something relatively innocuous. There remain the two other points: the delay and the Commonwealth preferences. It is relevant that it would be to the benefit of Germany, in particular, to accept the French proposals in these matters. The Germans would like to have two or three years' clear run in the French and Italian markets ahead of us, and they would certainly like to share in some of our Commonwealth preferences. It is therefore likely that we shall be pressed on both these points.

16. I feel sure my colleagues will agree that there can be no question of meeting in any way the French demand for a share in our preferences. It is in any case not a matter within our gift, and, if the demand comes in this form, it would be quite irreconcilable with the General Agreement on Tariffs and Trade. We must hold to the conception of the Commonwealth as a balanced system of rights and duties and not merely one of unilateral advantage to the United Kingdom. But, in the long run, I imagine we would argue that the Free Trade Area should have as one of its aims a closer association between the Commonwealth as a whole and Continental Europe, and it may be that this is a line of thought that we should develop.

17. So far as the delay in starting the tariff reductions is concerned, I am sure we must not accept this as a general principle. All our allies in Europe outside the Six are strongly opposed to it, and the Belgians and at any rate some of the Germans themselves regard it as a bad idea. But it may be possible to make special arrangements with France. Indeed, I am being driven to the conclusion that the only solution will be some special protocol for France. Already she has special conditions in the Treaty of Rome, which will have to be continued in the Free Trade Area. Every country in Europe would be prepared to make a special concession to France if only the French were prepared to accept it. At the moment they are entirely opposed, on the theoretical grounds that this would destroy the unity of the Six. Their real grounds are probably a reluctance to being further isolated and a fear that the offer of special terms would make the negative attitude seem even more ~~immovable~~. It will be a major question of tactics when, and in what way, we should float the idea of a special protocol for France if we decide that this is the right way to handle the problem.

18. The next two or three months should see the decision one way or the other—whether we can have a Free Trade Area or whether we have to abandon the project. One of the most important events will be Dr. Adenauer's visit to London, because Germany is in a key position and Dr. Adenauer alone appears to hold the key to German policy. I believe myself that what we should aim at is to get some sort of Free Trade Area off the ground on its first flight, even if this involves all sorts of limitations and conditions and some special treatment for France. Once it has made its first flight we can set about making it a really powerful and effective machine. If we try to achieve too much perfection in advance we may fail to get agreement altogether.

R. M.

*Office of the Paymaster-General, S.W. 1,
20th March, 1958.*