

PO-CH/NL/0504

PART A

Part A.

RESTRICTED

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Begins : 14/12/88
Ends : 8/11/89

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PO CH | NL | 0504.
Pt.A.

Chancellor's (Lawson) Papers -
European Community Fiscal Frontiers Controls
and Intra-Trade Statistics.

DD's : 25 Years

Phelan

28/2/96.

PO CH | NL | 0504.
Pt.A.

FROM: SUSIE SYMES
DATE: 14 DECEMBER 1988

PS/CHANCELLOR

*Thanks.
X is asked
what I
asked
for.*

cc: Sir Geoffrey Littler
Mr Byatt
Mr R I G Allen
Mr Gilhooly
Mr Mortimer

FISCAL APPROXIMATION - IFS STUDIES

X | The Chancellor asked about recent press reports of an IFS study on the EC proposals. I think this must be the recent IFS report for the Round Table of European Industrialists, attached. But for completeness, I attach other recent IFS work on this topic that the Chancellor may not have seen.

2. I also attach a copy of Lord Cockfield's speaking note at the 12 December ECOFIN.

Susie Symes
SUSIE SYMES

*See in
minutes re it.*

*PS I should like
to have an analysis
of the work done by you
& more help please
(p 42 of the IFS report) XX*

Extract from Financial Times

6 December 1988 Page 11

EC 'should agree single minimum rate for VAT'

By Guy de Jonquères

DIFFERENCES between rates of value added tax in the European Community can be prevented from distorting competition after 1992 if countries agree to set a common minimum rate, the Institute for Fiscal Studies states.

It says in a report prepared for the Round Table of European Industrialists that such a system would be preferable to the EC Commission's controversial proposal to group national VAT rates into two bands.

The institute argues that the commission's proposal is needlessly restrictive. It says action to stop countries undercutting each others' tax rates is all that is needed. It adds that they should remain free to set maximum rates.

The report also criticises the commission's plan for a clearing house to redistribute VAT revenues between national governments after internal EC

frontier controls are abolished.

It says the planned clearing house would reduce the incentive for governments to detect VAT fraud. It suggests that enforcement would be more effective if the EC created an information base to monitor members' trade with each other.

The institute says harmonisation of excise duty rates will be unavoidable after 1992 unless agreement is reached on alternative administrative arrangements.

It explains that different national excise rates could continue if tax stamps were used for dutiable goods or if the EC allowed excise rates to be set by regional groupings of countries with few common land frontiers.

Opening Up The Tax Frontiers. Institute for Fiscal Studies, Round Table of European Industrialists, 15 Rue Guimard, 1040 Brussels, Belgium.



of. ~~scribble~~

14/4

Jonathan
Ms Symes is going
to meet you today to
explain

This is getting silly
(see all the various promises
Ms Symes has given you,
which you have recorded!)
When will she give us
a reply?!

CTE will do
this/that work.

St

Jonathan.

10/15/3

Ms Symes is going to ~~call~~ talk to you about the attached on Friday.

That is when she will be in a position to tell us when we will be getting something on this.

The Reason for Friday is that M Brown is around on Friday + Ms Symes needs to consult her about this.

1 - 10/15/3

by 22/3
22/3

by 31/3



FROM: J M G TAYLOR

DATE: 4 January 1989

MS SYMES

cc Mr Byatt
Mr R I G Allen
Mr Gilhooly
Mr Mortimer

Jonathan
I spoke to Ms Symes.
She doesn't seem to think
we will get anything under the
end of February (she is away
most of Feb)

FISCAL APPROXIMATION - IFS STUDIES

The Chancellor was grateful for your note of 14 December, and the various enclosures. The IFS report for the Round Table of European Industrialists was indeed what he wanted.

- 2. I am returning (enclosed) your copy of this report. The Chancellor has noted, amongst the list of documents on page 42 of the report, a report of the group of IMSC tax experts on the Commission's proposals on indirect tax. He would be grateful for an analysis and evaluation of the key and most helpful points in this report. I should be grateful if you could take this forward.
- 3. The Chancellor had some comments on Lord Cockfield's speaking note, which I am minuting separately.

Jonathan
I have spoken to Ms Symes about this.
She hasn't forgotten about this, but she
keeps on getting work from her chiefs which they
feel is of a higher priority.
She is busy with ECOFIN work this week
but will have a look at this next week.
Maybe we should leave her alone this week
but have a word on Monday to try to get
a firm commitment of when this work will
be completed.

J M G TAYLOR

Jonathan
P.R. put on as
you
ppre.
2/

by 15/3



P Jefferson Smith
Deputy Chairman

Board Room
H M Customs and Excise
New King's Beam House
22 Upper Ground
London SE1 9PJ
Telephone: 01-382 5011

CONFIDENTIAL

CH/EXCHEQUER	
REC.	06 FEB 1989
ACTION	
COPIES TO	

Handwritten signature and note: (seen fax)

FROM: P JEFFERSON SMITH
DATE: 3 February 1989

CHANCELLOR OF THE EXCHEQUER

SINGLE EUROPEAN MARKET: INDIRECT TAXATION AND FRONTIER CONTROLS

At your meeting on 17 January, you discussed how the UK might respond in further discussions of tax harmonisation, e.g. to proposals for minimum rates. These issues are likely to come up in Brussels soon, and there is a need for instructions for these discussions. You may like to consult the Prime Minister and other Ministerial colleagues.

2. Discussions on the Commission's proposal for a VAT clearing house are taking place in Brussels on 8 February. The recent paper by the French rejecting the clearing house system and indications of a similar view from the Danes provide some encouragement that we can make early progress in our attempts to kill off the clearing house approach.

3. The Spanish Presidency intend that either Coreper or the Council's Financial Questions Group or both will discuss VAT rates and rate structure and excise duties shortly. Dates have not yet been fixed, but meetings are likely to be arranged at very short notice. We are doing our best to get as much notice as possible, but, certainly as far as Coreper is concerned, a few days' notice is the best we can expect. In these circumstances instructions for UKREP and Customs representatives in these discussions need to be settled in advance.

4. In view of the greater flexibility on the part of the Commission - in particular Mme Scrivener's ideas for making progress - it seems virtually certain that we shall be expected to take a line on a number of potentially sensitive issues. These are likely to include a VAT minimum standard rate (whether we could support one and if so, at what level?); a VAT reduced rate (could we support one, assuming it included a zero rate? on what basis should its coverage be settled?); and excise duties (what level of minimum rates would be acceptable to us?). Although the VAT clearing house may also be raised, the UK line is settled and

does not need to be re-considered.

5. Given our strongly argued case against any form of harmonisation, it could be argued that we should decline to take any part in the debate. But in Brussels this empty chair approach could do more harm than good. As the UK has been in the lead in exhorting the Commission to adopt a more flexible approach, a response that was too negative would be widely seen as being unconstructive and could lose us the initiative that your market forces approach has gained. Moreover, our refusal even to contemplate the smallest steps towards compromise (which could, as you suggested at your meeting on 17 January, lead to a highly satisfactory outcome for the UK), could strengthen the hand of those in the Commission and other Member States who favour a regulatory approach and leave the UK isolated.

6. We would therefore strongly recommend that those involved in discussions are authorised to take the cautiously open line set out in the attached letter, which we suggest you may wish to send to the Prime Minister and colleagues in OD(E). This sets out your negotiating tactics, including your proposed response to the sensitive issues set out above. It should not come as any great surprise to them.

7. This is a difficult area and we certainly do not want to reveal much of our hand at this early stage, but we believe it is essential that we should not stall the impetus towards more flexible, realistic solutions. We would be happy to discuss.

ph

P Jefferson Smith

Circulation:

Chief Secretary	Ms Symes	CPS
Financial Secretary	Mrs Chaplin	Mr Nash
Paymaster General	Mr Tyrie	Mr Finlinson
Economic Secretary	Mr Call	Mr Wilmott
Sir P Middleton		Mr P R H Allen
Mr Wicks		Mr Cockerell
Mr Lancaster		Mr Savins
Mr Scholar	(Sir D Hannay UKREP)	Mr Gaw
Mr R I G Allen		Mr Kent
Mr Gilhooly	(Mr Lavelle Cab Off)	Mr Knox

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Prime Minister

SINGLE EUROPEAN MARKET: INDIRECT TAXATION AND FRONTIER CONTROLS

A measure of progress is now taking place on this issue. Thanks to a considerable extent to the determined lead given by the UK towards a practical approach based on market forces, the deadlock on the Commission's tax approximation proposals seems to be breaking. The French have circulated proposals that follow our approach in rejecting the VAT clearing house and maintaining the destination system (that goods moving within the Community are, as now, zero-rated at export and bear the full tax at the rate in force in the country where they are consumed). Moreover, when I met Mme Scrivener, the new EC Commissioner in charge of this area, she made clear her view that the Commission needed seriously to re-think their approach.

2. The next stage of discussions is likely to focus on two separate, but related, issues. First is the question of administrative procedures (e.g. the VAT clearing house). Progress in this area is central to our approach to removing fiscal frontiers without tax approximation. Early discussions are in prospect and the wind seems to have moved rather more in our favour. The second issue is the more politically sensitive question involving VAT and excise rates and rate structures, including zero rates. Early discussions are likely in this area too.

3. While recent developments are encouraging, it is essential that we should continue to maintain the impetus towards flexible and realistic solutions to these difficult issues. Circumstances are currently favourable. The Spanish Presidency are allocating time for early discussions. However, our success in freeing up discussions - particularly of administrative issues - will inevitably mean that the politically sensitive issues are also raised. We cannot expect to achieve progress towards practical solutions if we are not also prepared to play a reasonably constructive part in considering issues of real concern to other Member States or in discussing the new ideas which are emerging as the Commission's monolithic approach breaks down - even if these raise awkward issues for us. Since discussions are likely to take place soon, we need to agree a negotiating line that will best guarantee our ultimate objectives.

4. Clearly we must avoid compromising any serious areas of principle - above all on zero rates - or giving away at this early stage of negotiations valuable bargaining points. On the other hand, if we refuse to discuss some of the new ideas that are

emerging, like VAT minimum rates, we could rightly be criticised by our Community partners for being inflexible (our principal argument against the Commission), inconsistent and obstructive. Moreover, we should lose the initiative which our determined stand in favour of market forces and realism has gained for us. I therefore propose a balanced approach to the sensitive issues, which are set out below and which are likely to be raised shortly in discussions.

5. If - but only if - these issues arise, and we are pressed to declare where we stand, these are the responses we should make:

(i) Could the UK accept a VAT minimum standard rate?

Under the UK's market-based approach, we see no need for either a rate band structure or a minimum standard rate. However, we acknowledge that other Member States who face greater cross-border shopping problems than the UK might see a minimum rate as some protection for their revenue. We would welcome the views of other Member States and, though sceptical, would not rule this out.

(ii) What minimum standard rate of VAT could UK accept?

If pressed we should note that the argument in favour of a minimum rate of VAT appears to be based on the need to prevent the competitive bidding down of VAT rates, so a minimum rate which preserved the status quo (i.e. 12%) would seem appropriate, rather than one which imposed inflationary price rises on a number of Member States. Further work would be needed on the implications.

(iii) What is the UK view of the suggestions made in reports of committees of the European Parliament of a VAT structure involving rate bands, but including a zero rate?

Rate bands are unnecessary under the UK market forces approach. As regards zero rates, it is essential that these should be retained on a permanent basis, with no question of a time-limited derogation.

(iv) What should be covered by reduced/zero VAT rates?

In keeping with the UK general approach, we see no need to establish a prescriptive list. Thus Member States would be free to tax at a reduced or zero rate any items that can currently be zero- or reduced-rated under the Sixth VAT Directive - (i.e. any items that are zero-rated in the UK for defined social reasons and which benefit the final consumer: in effect, all current UK zero-rated items).

(v) Could the UK accept any form of approximation of excise duty rates?

An unreal question. It is patently clear that the differences in rates of duties in different Member States are so great that approximation is not a realistic prospect. We need to look at practical ways of removing fiscal frontier controls in circumstances where excise duty rates differ considerably.

(vi) UK has suggested minimum excise duty rates for alcoholic drinks and tobacco products - at what levels?

The levels set would have to be sufficiently high to avoid serious damage to health - over the Community as a whole, not just in relation to a bare majority. Further work would be needed about the implications.

6. The overriding theme in answering questions of this sort would be that effort needs to be concentrated on agreeing administrative procedures for removing fiscal frontiers without the necessity for tax approximation.

7. You will see that though the proposed response is deliberately cautious, it does imply that we might be prepared to consider a minimum standard rate of VAT. Although this would mean a further lessening of our freedom of manoeuvre, we have to accept that our ability to zero rate or exempt supplies is already strictly circumscribed by the Sixth VAT Directive, (as the recent European Court judgment has amply illustrated). So this is essentially a matter of degree rather than of principle.

8. I am copying this to Geoffrey Howe and other colleagues in OD(E). Subject to any early comments you or they have, I would propose to authorise officials to approach the next stage of discussions in Brussels on the basis outlined above.

NL

R E S T R I C T E D

bf. 21/2



FROM: S M A JAMES
DATE: 16 February 1989

PS/CHANCELLOR

cc: PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
Sir P Middleton
Mr Wicks
Mr Lankester
Mr R I G Allen
Mr Culpin
Mrs Chaplin
Mr Tyrie
Mr Call

1/ your work X

PS/IR

PS/C&E
Mr Jefferson-Smith - C&E
Mr Nash - C&E
Mr Wilmott - C&E
Mr P R H Allen - C&E

Sir D Hannay - UKREP
Mr Lavelle - Cabinet Office

INDIRECT TAX HARMONISATION : DISCUSSIONS IN BRUSSELS

The Economic Secretary has seen Mr Jefferson-Smith's minute of 13 February, and your note of 14 February.

2. He agrees with the Chancellor and Mr Jefferson-Smith that it would be valuable to circulate the technical paper to the Commission and other Customs Administration. The Economic Secretary has commented that we should also consider launching it publicly and getting the *[kudos]* it deserves.

X

S M A JAMES
Private Secretary



P Jefferson Smith
Deputy Chairman

Board Room
H M Customs and Excise
New King's Beam House
22 Upper Ground
London SE1 9PJ
Telephone: 01-382 5011

FROM: P JEFFERSON SMITH
DATE: 28 FEBRUARY 1989

ECONOMIC SECRETARY

Thanks
PSO attends post 10.15 date of 16/2; has also
the drugs brief.

INDIRECT TAX AND FRONTIER CONTROLS IN THE SINGLE MARKET: PUBLIC PRESENTATION AND BRIEFING OF MEPs

1. Now that the Prime Minister has agreed that we can circulate our technical paper on indirect tax in the Single Market, we need to settle the matter of public presentation of both the technical proposals (on which your Private Secretary minuted PS/Chancellor on 16 February) and of our separate EC drugs brief.

2. The first question to be resolved is whether they should be treated together or separately. In view of the different approach and message of the two papers - (UK proposals to remove fiscal frontiers in one; UK giving practical reasons why preventive controls at internal frontiers cannot be removed in the other) - we

Distribution: Chancellor ✓
Paymaster General
Sir P Middleton
Mr Wicks
Mr Lankester
Mr R I G Allen
Mr Culpin
Ms Symes
Mrs Chaplin
Mr Tyrie
Mr Call

CPS
Mr Nash
Mr Finlinson
Mr Wilmott
Mr P R H Allen
Mr Brown
Mr Cockerell
Mr Knox

PS/Inland Revenue
Sir D Hannay (UKREP)
Mr Lavelle (Cabinet Office)
Mr Kerr (FCO)

would recommend strongly that they should be kept separate. Otherwise the different messages will not get over clearly. In particular, there is a risk that our positive message on the removal of fiscal frontiers will be obscured.

3. Circulation within UK We propose to send copies of first the drugs brief and, a week or so later, the indirect tax paper to the clerks to the Select Committee on European Legislation and Treasury and Civil Service Select Committee respectively. We have already arranged for a copy of the drugs brief to be placed in the libraries of both Houses and will do the same for the indirect tax paper. We had proposed to treat the drugs brief as being an essentially defensive document, which we should make available on request. We would therefore not propose to initiate any publicity. Similarly, a high profile approach to the indirect tax paper is inappropriate. But as we are going to circulate it at official level within the Community, it seems a sensible precaution to ensure that the Select Committees have it.

4. Circulation within EC The Chairman will send copies of both papers to his EC colleagues and copies will also be sent to appropriate Commission and Council officials. We have already circulated copies of the drugs brief within UKREP and to UK embassies in EC countries. We propose to do the same with the indirect tax paper.

5. Sir David Hannay is keen that there should be an early briefing of MEPs on both sets of issues. As far as the drugs brief is concerned, we suggest that a copy should be sent to all UK MEPs very shortly. This might be accompanied by a letter from you to the leader of the EDG and of the Labour Group. If you agree with this we will prepare a draft for you.

6. It is important that our indirect tax proposals are in the minds of UK MEPs before what may well be a vital European Parliament debate on the Commission's proposals in mid-April. However, we want this to be relatively fresh in their minds and separate from the drugs brief. Our paper is probably too technical to be of direct interest to many MEPs. The key message is that the UK has developed procedures that would allow the removal of fiscal

frontiers without tax approximation. We consider, therefore, that a general briefing on the UK approach, including a precis of the technical paper, would be most effective. There are, of course, a number of MEPs who are interested in the technical details. They could be given the technical paper if they wanted it: in particular, you might send a copy to Ben Patterson.

7. This briefing should be in the hands of MEPs early in April. We suggest that its effectiveness would be greatly reinforced if it was handed over as part of an oral briefing by a Treasury Minister. This would involve a one day trip to Strasbourg or wherever the Parliament was in April. If you would be prepared to do this, we will see what can be set up.

8. If you are content with these courses of action, we shall press ahead as suggested.

PK ✓

P JEFFERSON SMITH



cc : Chancellor ✓
Paymaster General, HMT
Sir P Middleton, HMT
N Wicks Esq, HMT
T Lankester Esq, HMT
R I G Allen Esq, HMT
R P Culpin Esq, HMT
Ms Symes, HMT
Mrs Chaplin, HMT
A Tyrie Esq, HMT
M Call Esq, HMT

CPS

P Nash Esq, HM Customs & Excise
C Finlinson Esq, HM Customs & Excise
P Wilmott Esq, HM Customs and Excise
P R H Allen Esq, HM Customs & Excise
R Brown Esq, HM Customs & Excise
B Cockerell Esq, HM Customs & Excise
B Knox Esq CB, HM Customs & Excise

PS/Inland Revenue

R G Lavelle Esq CB, Cabinet Office
J O Kerr Esq CMG, FCO



OFFICE OF THE UNITED KINGDOM
PERMANENT REPRESENTATIVE
TO THE EUROPEAN COMMUNITIES
ROND-POINT ROBERT SCHUMAN 6
1040 BRUSSELS

FROM THE PERMANENT REPRESENTATIVE

P Jefferson Smith Esq
HM Customs and Excise
King's Beam House
39-41 Mark Lane
LONDON EC3R 7HE

CH/EXCHEQUER	
REC.	-3 MAR 1989
ACTING	EST
LETTER TO	

TELEPHONE 230 62 05

1 March 1989

PPS with you!
RIG. ALLEN 1/3

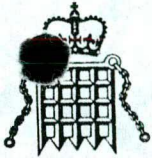
Dear Peter,

INDIRECT TAX AND FRONTIER CONTROLS IN THE SINGLE MARKET : PUBLIC PRESENTATION AND BRIEFING OF MEPS

1. Thank you for sending me a copy of your minute of 28 February to the Economic Secretary. This follows up, admirably if I may say so, the points we identified at the Cabinet Office last week.
 2. I am sending copies of the technical paper to Madame Scrivener's Chef de Cabinet, to the two UK Chefs de Cabinet, to David Williamson, to Joly Dixon in Delors' Cabinet and to Adrian Fortescue because of his frontier controls responsibilities.
 3. There is just one point which has not, I think, come out quite right, the briefing of MEPs on our approach to indirect tax issues. I fear that briefing MEPs during the April Plenary session will be far too late to enable them to make the best use of the points we are making. Moreover I would not recommend the Economic Secretary to go to Strasbourg during the April session. He would inevitably be drawn into the zero rate fracas which is likely to be one of the most hotly disputed issues in the debate on the Commission's proposals and there is a real risk of his presence being interpreted as high pressure British government lobbying on zero rates which would certainly be counter-productive. If, contrary to our hopes, the EP reject the zero rates amendment, then Mr Lilley's presence would be seen as positively humiliating.
3. My alternative suggestion is as follows:
- (i) A written brief should be prepared promptly and sent to all 81 UK MEPs by the Economic Secretary
 - (ii) The Economic Secretary should offer an oral briefing in London to EDG MEPs.

L. Lilley
David Hannay
D H A Hannay

/cc:



HM CUSTOMS AND EXCISE
CUSTOMS DIRECTORATE
DORSET HOUSE, STAMFORD STREET
LONDON SE1 9PS
01-928 0533 2138
GTN 2523

ECONOMIC SECRETARY

FROM: MARTIN BROWN
CD DIVISION E

DATE: 2 MARCH 1989

PUBLICITY ON DRUGS BRIEF 1992

You will have seen the attached article in the Times quoting from our Drugs Brief. It derives from an informal, unattributable press briefing on a variety of issues, given in Brussels by UKREP. The press pricked up their ears particularly on the drugs front.

The article is generally helpful, though it misreports one statistic in our Brief. The 1988 figures do not show that 44% of drugs come from the EC:

- a) 23% of total drugs come from EC (ie a drop from 41% in 1987); but
- b) there was a 44% increase in the weight of the EC share.

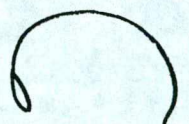
Copies of the Drugs Brief were laid in the Libraries of both Houses on 28 February.

cc.	Chancellor	Ms Symes	<u>Internal</u>
	Chief Secretary	Mr Gilhooly	CPS
	Financial Secretary	Mr Michie	Mrs Strachan
	Paymaster General	Mr Tyrie	Mr Jefferson Smith
	Sir P Middleton	Mr Call	Mr Nash
	Mr Wicks	Mrs Chaplin	Mr Savins
	Mr Lankester	Treasury Press Office	Mr Walton
	Mrs Case	Mr W Parker (Cab. Off.)	Mr Allen
	Mr R I G Allen	Mr Norgrove (UKREP)	Mr Tweddle
	Mr Culpin		Mr Knox
			Mr Hammond

If the press ask for a ministerial comment on the Drugs Brief figures, we suggest:

"Drugs smuggling across our internal borders with other EC countries is a major threat to our society. So we cannot just abandon all customs checks after 1992.

The UK actively supports plans to strengthen the EC's external defences against drugs. This will mean raising enforcement standards across the Community to a uniformly high level and promoting even greater co-operation between EC countries. We are anxious to achieve real progress here which could allow us to scale down checks at the internal frontier."



MARTIN BROWN
CD DIVISION E

R E S T R I C T E D



FROM: S M A JAMES
DATE: 2 March 1989

MR JEFFERSON-SMITH C&E

cc: PS/Chancellor ²
PS/Paymaster General
Sir P Middleton
Mr Wicks
Mr Lankester
Mr R I G Allen
Mr Culpin
Mr Gilhooly
Mr Gieve *
Mrs Brown
Ms Symes
Mrs Chaplin
Mr Tyrie
Mr Call

PS/C&E*
Mr Nash - C&E*
Mr Finlinson - C&E*
Mr P R H Allen - C&E*
Mr Brown - C&E*

PS/IR*

Sir D Hannay - UKREP*

*with Mr Allen's minute of 1 March

INDIRECT TAX AND FRONTIER CONTROLS IN THE SINGLE MARKET : PUBLIC PRESENTATION AND BRIEFING OF MEPS

The Economic Secretary was grateful for your minute of 28 February. He has also seen Mr Allen's note of 1 March.

2. He agrees that the drugs brief and technical paper should be treated separately, indeed he wonders whether we need to send the drugs brief out at all. He had regarded it as essentially an internal speaking note.

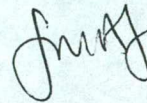
3. The Economic Secretary has commented that if we send Customs' technical paper to MEPS, the TCSC and the clerks to the Select Committee on European Legislation (as well as other Customs

R E S T R I C T E D

administrations and Commission officials), it may well seep into the media. No.10 may well raise this and we need to address the question ourselves first.

4. The Economic Secretary wonders whether we want to present the paper to the media in this indirect fashion or to make a big splash (which he would favour if it does not cut across our negotiating tactics) or to give a low key but still managed release direct to the press. If a decision were made in favour of a high profile presentation, the best way to get such coverage would be a speech by the Chancellor. But if we distributed the document in the UK the speech would have to be made pretty soon thereafter.

5. The Economic Secretary would welcome views on the possibility of publicising the paper.



S M A JAMES
Private Secretary



P Jefferson Smith
Deputy Chairman

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Telephone: 01-382 5011

Smith
PMJ
FROM: P JEFFERSON SMITH
DATE: 6 MARCH 1989

ECONOMIC SECRETARY

INDIRECT TAX AND FRONTIER CONTROLS IN THE SINGLE MARKET: PUBLIC PRESENTATION AND BRIEFING OF MEPS

Your Private Secretary's note of 2 March raised a number of points in relation to my minute of 28 February. Sir David Hannay has also made some comments, especially in relation to handling MEPS.

2. As you will have seen, the drugs brief has already received press comment. I understand that it has attracted considerable interest in Brussels and a number of requests for additional copies have been received there. I think we shall have to swim with the tide on this: ie we should continue to provide copies on request, but not give the brief a higher profile.

Distribution: Chancellor ✓
 Paymaster General
 Sir P Middleton
 Mr Wicks
 Mr Lankester
 Mr R I G Allen
 Mr Culpin
 Mr Gilhooly
 Mr Gieve
 Mrs Brown
 Ms Symes
 Mrs Chaplin
 Mr Tyrie
 Mr Call

CPS
 Mr Nash
 Mr Finlinson
 Mr Wilmott
 Mr P R H Allen
 Mr Brown
 Mr Cockerell
 Mr Savins
 Mr Knox
 Mr Hammond
 Mr Oxenford

PS/Inland Revenue
 Sir D Hannay, UKREP

3. The technical paper on indirect tax in the Single Market has already obtained a rather garbled mention in "the Guardian" on 3 March, as a result, we understand, of some generalised briefing by UKREP. We agree with Mr R I G Allen's note of 1 March that giving this a high media profile, especially if it were to involve Ministers, would run directly counter to what the Chancellor said to the Prime Minister in his note of 22 February. The paper is technical, written by officials essentially for officials in other EC administrations and the Commission. Although this is a matter of political judgment, we would question whether a higher political profile is appropriate at this stage.

4. The paper will inevitably become public knowledge in due course. The relevant Parliamentary committees are likely to consider it discourteous of us not to let them have copies. To avoid this, we would suggest that we should send copies to the clerks shortly. Moreover, there will be wider interest in the UK. Trade bodies with whom we have regular discussions will expect to be informed of its contents, and there is no reason why they should not have copies. In handling the media, there seem two possible approaches: one would be for Customs to issue a low key press notice in the near future, informing No. 10 that we are doing so; the other is simply to be ready with defensive briefing, so that our Press Offices are able to explain what the status of the paper is and who it has gone to (but not to give it general release). We think the latter is as far as we really need to go.

5. As far as briefing MEPs is concerned, I see no reason to dissent from Sir David Hannay's latest advice that a written brief should be provided and that you might brief EDG MEPs in London. However, in view of your regular dealings with Ben Patterson MEP, we cannot see any real objection to your sending him a copy of the technical paper, provided that the status of the paper is made clear. If you agree, we shall provide a suitable draft.

6. We would be happy to discuss if you thought this helpful.

PS

P JEFFERSON SMITH

R E S T R I C T E D



FROM: S M A JAMES
DATE: 8 March 1989

MR JEFFERSON-SMITH C&E

cc: PS/Chancellor ²
PS/Paymaster General
Sir P Middleton
Mr Wicks
Mr Lankester
Mr R I G Allen
Mr Culpin
Mr Gilhooly
Mr Gieve
Mrs Brown
Ms Symes
Mrs Chaplin
Mr Tyrie
Mr Call

PS/C&E
Mr Nash - C&E
Mr Finlinson - C&E
Mr P R H Allen - C&E
Mr Brown - C&E

PS/IR

Sir D Hannay - UKREP

INDIRECT TAX AND FRONTIER CONTROLS IN THE SINGLE MARKET : PUBLIC PRESENTATION AND BRIEFING OF MEPS

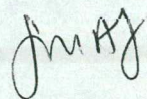
The Economic Secretary was grateful for your minute of 6 March. He has also seen Sir David Hannay's letter to you of 1 March.

2. He assumes your reason (your paragraph 3) for questioning whether a high profile for the technical paper now^{is} appropriate is to do with our negotiating position. He would welcome Sir David Hannay's views on this.

3. He agrees with Sir David Hannay's suggestion that he should brief EDG MEPs orally in London and send a written brief to all UK MEPs. He agrees with your proposal that we also need a written brief for press offices (although he has commented that this should not be purely defensive).

R E S T R I C T E D

4. He agrees that he should write to Ben Patterson MEP enclosing a copy of the technical paper. He would be grateful for a suitable draft.



S M A JAMES
Private Secretary

RESTRICTED

FROM: R I G ALLEN
DATE: 9 MARCH 1989

PS/ECONOMIC SECRETARY

cc PS/Chancellor
PS/Paymaster General
Sir P Middleton
Mr Wicks
Mr Lankester
Mr Culpin
Mr Gilhooly
Mr Gieve
Mrs Brown
Ms Symes
Mrs Chaplin
Mr Tyrie
Mr Call

PS/C&E
Mr Jefferson Smith, C&E
Mr Nash, C&E
Mr Finlinson, C&E
Mr P R H Allen, C&E
Mr Brown, C&E

PS/IR

Sir D Hannay, UKREP

**INDIRECT TAX AND FRONTIER CONTROLS IN THE SINGLE MARKET: PUBLIC
PRESENTATION AND BRIEFING OF MEPS**

I gather you are arranging a meeting next Monday to discuss this subject, on which there has been a good deal of recent minuting. In advance of that, perhaps I could pass on one or two points which were put to me by Sir David Hannay.

2. On drugs, it was important to get Customs' brief to MEPs without delay: no particular need for the document to be issued undercover of a letter from the Economic Secretary.

3. On the handling of the technical paper on VAT/excises, the important point to stress was that it was a working document rather than a formal proposal. The distinction between a Government paper and a paper by officials would not wash, particularly because Ministers had seen it and had agreed to it being circulated.

4. Sir David reiterated the advice in his letter of 1 March to Mr Jefferson Smith that a visit by the Economic Secretary to Strasbourg would be counterproductive. The better option would be to give an oral briefing in London to EDG MEPs, using the proposed general tax/drugs brief - currently in draft - as a text.

5. It would be useful for a Treasury Minister to include some general references to Customs' latest thinking on indirect tax approximation in a speech prior to the ECOFIN discussion on 17 April. It should be feasible to weave this into the fabric of a post-Budget speaking engagement, and give Customs' ideas a bit of a puff. One possibility would be the Paymaster General's speech to the IFS Tax Conference on 7/8 April, when the main theme will be the Single Market.

12/7

R I G ALLEN



FROM: S M A JAMES
DATE: 16 MARCH 1989

PS/CHANCELLOR

cc:

PS/Paymaster General
Sir P Middleton
Mr Wicks
Mr Lankester
Mr Culpin
Mr Gilhooly
Mr Gieve
Mrs M Brown
Ms Symes
Mrs Chaplin
Mr Tyrie
Mr Call

PS/C&E
Mr Jefferson-Smith - C&E
Mr Nash - C&E
Mr Finlinson - C&E
Mr P R H Allen - C&E
Mr M Brown - C&E

PS/IR

Sir D Hannay - UKREP

I see some advantage in giving a non-political answer to the IFS speech on 7/8 April. Agree with EST's suggestions? (I understand that PMG may have privately agreed with you separately that it might actually be best to make a speech pre- ELOFIN - i.e. his speech at the IFS conference on 7/8 April).

INDIRECT TAX AND FRONTIER CONTROLS IN THE SINGLE MARKET : PUBLIC PRESENTATION AND BRIEFING OF MEPS

The Economic Secretary has discussed the recent papers with Treasury and Customs officials.

2. The Economic Secretary agrees with Customs that the technical paper on frontier controls and the drugs brief should be treated separately. Copies of the technical paper and the drugs brief have already been sent to Commission officials, heads of Customs administrations, the libraries of both Houses and the Clerks to the Select Committee on European Legislation, the Treasury and Civil Service Select Committee and the House of Lords Select Committee on the European Communities.

3. The Economic Secretary agrees with officials that Sir David Hannay should send the drugs brief to the EDG and to Labour MEPs for their information. He agrees also that a brief on tax approximation, which would include the proposals in the

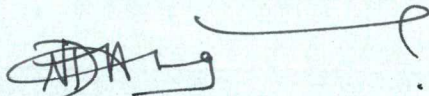
technical paper, should be sent to all UK MEPs. It would be best to cover the main points of this paper in a more general brief rather than sending MEPs the paper itself. A brief would allow us to highlight the points on which we wished MEPs to focus. The brief would be sent in the week beginning 3 April and in the following week the Economic Secretary would brief members of the EDG orally in London. This would be around a week before April ECOFIN (17 April) and the April plenary session.

4. It was agreed that if the UK press asked for copies of the technical paper these should be supplied. Customs have provided IDT with Q&A briefing.

5. The Economic Secretary discussed with officials the timing of a possible Ministerial speech on the general UK approach to frontier controls. A suitable occasion for such a speech before April ECOFIN might be the Paymaster's speech at the IFS conference on 1992 and beyond in Oxford on 7/8 April. A speech before ECOFIN on 17 April might help to influence the Presidency. However there were other and arguably better ways of achieving this less directly. The Commission and other member states were already aware of our proposals through lobbying at official level.

6. On balance the Economic Secretary favoured a speech after ECOFIN unless there seemed compelling reasons for bringing this forward and making a pre-emptive strike. In the speech we could highlight the fact that other member states had difficulties with the Commission's proposals but that we had been working on practical ways to achieve abolition of frontier controls without the need for tax approximation. As with the ECU Treasury Bill programme, this showed the UK taking concrete, practical steps towards a single European market.

7. The Economic Secretary would be grateful for the Chancellor's views on presentation and in particular on the proposal of a Ministerial speech after April ECOFIN.


H S M A JAMES

Private Secretary



FROM: J M G TAYLOR
DATE: 17 March 1989

PHP

PS/ECONOMIC SECRETARY

cc PS/Paymaster General
Sir P Middleton
Mr Wicks
Mr Lankester
Mr Culpin
Mr Gilhooly
Mr Gieve
Mrs M Brown
Ms Symes
Mrs Chaplin
Mr Tyrie
Mr Call

PS/C&E
Mr Jefferson Smith - C&E
Mr Nash - C&E
Mr Finlinson - C&E
Mr P R H Allen - C&E
Mr M Brown - C&E

PS/IR

Sir D Hannay - UKREP

**INDIRECT TAX AND FRONTIER CONTROLS IN THE SINGLE MARKET:
PUBLIC PRESENTATION AND BRIEFING OF MEPS**

The Chancellor has seen your note of 16 March.

2. He sees some advantage in the Paymaster General giving a wholly non-polemical explanation of the UK's general approach in his IFS speech on 7/8 April. That apart, he agrees with the Economic Secretary's conclusions.

J

J M G TAYLOR

FROM: P R H ALLEN
Departmental Planning Unit

DATE: 13 April 1989

PS/CHANCELLOR

3 months to go

PHP

**REPORT OF THE GROUP OF THE INTERNAL MARKET SUPPORT COMMITTEE
(IMSC) EXPERTS ON THE COMMISSION'S PROPOSALS ON INDIRECT TAX
- 16 DECEMBER 1987**

a very long time go!

1. I understand that the Chancellor asked for a note on the above report, which was referred to in the bibliography in the report prepared by the Institute for Fiscal Studies for the Round Table of European Industrialists entitled "Opening up the Tax Frontiers - The Future of Indirect Taxes in Europe". A summary is attached as an annex.

2. The report examines the Commission's package of proposals for the approximation of indirect tax rates and the harmonisation of indirect tax structures, published in August 1987. In particular, it examines the likely effects on pricing, consumption and employment in the European cigarette industry. It has nothing new to say.

3. It should be borne in mind that the report was prepared in 1987 and, in respect of the cigarette industries, relies on information published in 1985.

W. Baillie
PP.
P R H ALLEN

Circulation:

PS Paymaster General	Mr Culpin	Chairman
PS/Financial Secretary	Mr Gilhooly	Mr Jefferson Smith
PS/Economic Secretary	Mr Gieve	Mr Nash
Sir P Middleton	Ms Symes	Mr Wilmott
Mr Scholar	Mr Michie	Mr Knox
Mrs Chaplin		Mr Oxenford
Mr Tyrie		Mr Publicover - FCO
Mr Call		Mr Norgrove - UKREP
Mr Lancaster		
Mr R I G Allen		

SUMMARY OF THE REPORT OF THE GROUP OF IMSC TAX EXPERTS ON THE COMMISSION'S PROPOSALS ON INDIRECT TAX**GENERAL**

1. The IMSC express complete support for the aims of the Commission's proposals and pledges to support the progress towards completion of the single market and the removal of fiscal frontiers in every way they can.

VAT

2. They generally support the proposals for the approximation of VAT rates but make two points. First, they consider approximation unnecessary in respect of transactions unlikely to be traded across frontiers, eg. land and buildings, and urges the Commissions to review this area. Secondly, whilst recognising that harmonisation is necessary between adjoining countries, believes a wider divergence of rates could be tolerated in other where countries are not adjacent.

VAT CLEARING HOUSE

3. They generally support the Commission's outline proposals for a VAT clearing mechanism. However, they had a number of specific comments they hoped the Commission would examine. Their main concerns are: the exchange rates to be used by traders for determining VAT credits; the need for recognition of the electronic "paperless" environment when standardising audit trails and information requirements; that the scope for fraud has not been fully appreciated; the potential cost and burden of administration; and that credit for VAT on intra-community transactions should be given automatically in the same way as credit for VAT on domestic transactions.

4. They consider that the administration of the Clearing House could be greatly reduced if VAT on "intra-Group" transactions were omitted.

EXCISE

5. The IMSC, in noting that the Commission take no account of the effect of changes in consumption or trans-frontier trade resulting from their proposals, believes the effects on pricing, consumption and employment could be considerable, and call into question the validity of the proposals and the estimated budgetary effects.

6. They reach their conclusion on the basis of the cigarette tax harmonisation proposals, an area in which they have access to information and expertise.

7. They consider that there will be changes in revenue and sales volumes which will have a considerable impact on spending patterns, production and employment in various countries, which are unlikely to be acceptable to Governments in the timescale envisaged. Their research indicates 370,000 people may be employed full time on the growing, manufacturing and the distribution or retailing of tobacco products in Italy, Portugal, France, Spain and Greece, with just over 200,000 hectares of land under tobacco cultivation in the five countries. They estimate that resulting losses of employment might be equivalent to 65,000 full time jobs, more than two-fifths of them in Greece and 17 1/2 per cent of the total volume of tobacco related employment in the five countries. Accordingly, they ask the Commission to consider a longer timescale in the area of cigarette taxation, with a possibility of a preliminary harmonising of rates with three separate groupings; the original "six"; UK, Ireland & Denmark; Greece, Spain & Portugal.

8. For alcoholic beverages, they believe that the proposals are based on budget balancing which may be based on incorrect assumptions that no changes in spending pattern will be caused by the price changes proposed. They therefore opine that, in the short term, some degree of flexibility of rates could be accommodated without unacceptable trade distortions.

9. Finally, they support the principle of commercial movements of excisable goods being controlled via a system of linked bonded warehouses with no controls at the frontiers, and some

control (not necessarily at the frontier) to ensure that cross border trading stays within acceptable bounds.



QUEEN ANNE'S GATE LONDON SW1H 9AT

Our Ref: DDA/89 26/15/2

9 May 1989

Dear Nigel,

INTRA-COMMUNITY FRONTIER CONTROLS

One of my concerns about the proposed abolition of intra-Community frontier controls has been the effect that it will have on the United Kingdom's ability to comply with the relevant provisions of the two United Nations Conventions which govern licit trade in narcotic drugs and psychotropic substances. This has hitherto tended to take second place on the political stage to their implications for the illicit trade in drugs, but it is nonetheless important and we need to make sure the issues to which it gives rise are properly addressed by our EC partners.

A particular issue is whether advantage should be taken of the possibility which exists under the two United Nations Conventions of the EC becoming a single territory for the purposes of the relevant provisions of those Conventions. If this were done, the licit trade in drugs between EC countries could cease to be governed by the Conventions, which would operate only with regard to extra-Community trade. Intra-Community trade can be regulated by some more streamlined arrangements which would not rely on Customs controls at the frontier. A suitable forum in which to discuss this matter is the EC Ad Hoc Working Group on Drug Addiction. At a meeting in January the United Kingdom delegation proposed that the Working Group might consider establishing a sub-group to examine the feasibility of the EC becoming a single territory after 1992, and how this might be practically achieved. This was supported in principle by several Member States and the Presidency agreed to the matter being discussed at the subsequent meeting, for which the United Kingdom would provide a paper.

The enclosed draft paper is the product of discussions between our officials and takes account of comments made by the Official Committee on European Questions on an earlier draft. If you and David Young - to whom I am copying this letter - are content with the paper I will arrange for it to be submitted to the Ad Hoc Working Group for discussion at its next meeting towards the end of this month. To meet the Group's timetable it would be helpful if you could let me know by Thursday, 11 May whether you are content for the paper to go forward.

CH/EXCHEQUER	
REC.	- 9 MAY 1989
ACTION	MR NASH - CTE
COPIES TO	EST, PMG SIR P MIDDLETON, MR WICKS MR LAWRENCE, MR RIG ALLEN MRS BROWN, MS SYMES MRS CHAPLIN, MR TYRIE MR LAWRENCE - CTE MR JEFFERSON-SMITH - CTE

Lawson
Young

The Rt Hon Nigel Lawson, MP. MR RIG ALLEN - CTE

IMPLICATIONS OF SINGLE MARKET FOR INTERNATIONAL CONTROLS OVER
NARCOTIC DRUGS AND PSYCHOTROPIC SUBSTANCES

Paper by the United Kingdom

This paper recommends the establishment of a working group to examine how member states of the Community may comply with the provisions relating to the international licit trade in drugs contained in the United Nations Single Convention on Narcotics Drugs 1961, as amended by the 1972 Protocol, and the Convention on Psychotropic Substances 1971, in the new circumstances which will apply with the establishment of the internal market foreseen in the Single European Act.

International controls

2. Very broadly, Article 19 of the Single Convention provides that each country or territory shall furnish to the International Narcotics Control Board (INCB) each year estimates of the quantities of narcotic drugs to be consumed for medical and scientific purposes, of those to be utilised for the manufacture of other drugs and preparations and of those to be held as essential stocks. Article 21 of the Convention provides that the total quantities of each drug manufactured or imported by any country or territory shall not exceed the amount of the estimate established for that drug. Article 31 of the Convention provides that the import and export of any drug shall be forbidden except under licence. An export licence may be issued only where the competent authority of the importing country concerned has (a) established a sufficient estimate for the quantity to be imported; and (b) issued an import certificate in respect of importation.

3. The system of control under the Psychotropic Substances Convention is simpler in that there is no estimates system with which to comply. But Article 12 of the Convention provides that the import and export of substances specified in Schedules I and II shall be subject to control measures broadly similar to those

provided under Article 31 of the Single Convention. In addition **Article 13** provides that Parties shall take measures to prevent the export of any substance in respect of which the importing state has given notice that it has prohibited the importation of the substance.

4. To help ensure that Parties to these Conventions comply fully with their obligations, as well as to give an overview of the international licit manufacture and trade in narcotic drugs and psychotropic substances, Parties are required to forward periodical statistical returns to the INCB.

Operation of controls

5. The system of control established under the 1961 Convention is a complicated one, and the more so because of the estimates system; that under the 1971 Convention is more straightforward. But both have worked satisfactorily over many years and there is no pressure for either Convention to be amended in this regard.

6. The experience of the United Kingdom has been that the **estimates system** can only be made to work effectively under a regime which prohibits the importation of drugs not manufactured in the United Kingdom. This regime has been devised in the interests of preventing diversion of licit supplies on to the black market, rather than of protecting UK manufacturers. If wholesalers were permitted freely to import drugs into the United Kingdom, it would be very difficult to ensure the security of all shipments. The working of the estimates system would also become very much more complex.

7. As regards the **import/export system** of control, the United Kingdom experience has been that this has worked well but only because of the efficacy of the controls operated by HM Customs and Excise on all goods which are imported and exported.

8. In so far as the establishment of the internal market foreseen in the Single European Act might result in a reduction of routine Customs controls exercised by member states over international intra-Community trade it may be difficult for member states individually to comply with their obligations under the Single Convention with regard to the estimates system of control or, under both Conventions, with regard to the import/export system of control.

9. Each Convention provides for two or more Parties to notify the Secretary-General that, as the result of the establishment of a customs union between them, those Parties constitute a single territory for the purposes of those articles which relate to the estimates system (1961 Convention only) and the international trade. It would therefore be legally possible for the European Community to notify the Secretary General that it wishes to be treated as a single territory in future for the purposes of the relevant articles. The result of this would be that a single administrative body - presumably the Commission - would become the competent authority for the purposes of the two Conventions and would be responsible, in collaboration with the national drugs authorities of each State, for the estimates system of control and for the making of returns to the INCB etc. Matters for decision would be the extent of the body's competence to direct policy and its accountability to member states through the Council of Ministers.

Proposal for Working Group

10. If it is agreed that it would be prudent at this stage to examine the feasibility of the Community's becoming a single territory for the purposes of the relevant articles of the 1961 and 1971 Conventions, the United Kingdom would suggest that this might conveniently be done by a working group of the Ad Hoc Committee on Drug Addiction with the following terms of reference:

"To examine whether, in order to facilitate continued compliance by member states with the provisions of Articles 19, 20, 21 and 31 of the Single Convention on Narcotic Drugs 1961 and Article 12 of the Psychotropic Substances Convention 1971 in the new circumstances which will apply with the establishment of the international market foreseen in the Single European Act, it would be advantageous for them to constitute a single territory and, if so, to make recommendations as to how this might most effectively be achieved."

11. On the **membership** of the Working Group we would suggest that it comprise an expert from each member state who has practical experience of administering the relevant systems of control together with officers of the relevant directorates of the Commission. It might also be desirable to involve the Secretariat of the INCB in the discussions, if not from the outset at least from an early stage. When this proposal was recently discussed with him informally, Mr Bahi, the Board's Secretary, said he would willingly assist in any way he could.

12. As to the **Chairmanship** of the Working Group the United Kingdom believes it is desirable that the person appointed should serve in a personal capacity throughout the life of the group and might not, therefore, be the representative of the Presidency.

Home Office
C5 Division
50 Queen Anne's Gate
London SW1H 9AT

April 1989
D:L1.18



P Jefferson Smith
Deputy Chairman

CHANCELLOR

Board Room
H M Customs and Excise
New King's Beam House
22 Upper Ground
London SE1 9PJ
Telephone: 01-382 5011

Ch. Content to write as proposed?
OK
15/5

FROM: P JEFFERSON SMITH
DATE: 15 MAY 1989

PP. 17

behind

INTRA-COMMUNITY FRONTIER CONTROLS: HOME SECRETARY'S NOTE OF 9 MAY

The paper enclosed with the Home Secretary's note of 9 May seeks a possible solution to the problem of compliance with our obligations under the UN Conventions for the control of licit drugs after the completion of the single market. It has been under consideration for some months at official level and has been discussed at EQO.

2. This Home Office initiative arises from concern that, without routine Customs controls on legitimate trade, the UK would be unable to comply with obligations under the UN Conventions of 1961 and 1971 in connection with licit trade in narcotic drugs and psychotropic substances. Creating a single, EC territory for the purposes of the Conventions has an attraction in that obligations need only be met in respect of movements across the external frontier. However, there are countervailing disadvantages. By proposing that the Community becomes a single territory for the purpose of these Conventions, it raises the question of an extension of Community competence, and this is probably not the right time to do so. The Community already has competence on the duty elements of licit drugs but not on

<u>Distribution:</u>	Economic Secretary	CPS
	Paymaster General	Mr Nash
	Sir P Middleton	Mr D Walton
	Mr Wicks	
	Mr Lankester	
	Mr R I G Allen	
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	Ms Symes	
	Mrs Chaplin	
	Mr Tyrrie	

licensing (licences are granted by the Home Office and controlled by Customs at the point of entry). If it is finally agreed that the EC should form a single geographical territory to regulate licit trade, the Commission would assume competence for any licensing arrangements and these would be carried out at the external frontiers.

3. In spite of this, we may still be able to impose our own internal frontier control under Article 36 but would need to consider whether we wished to maintain a control system for licit drugs only. Thinking on internal frontier controls or alternative systems for MCAs, COCOM and other prohibitions and restrictions has not yet been finalised.

4. We believe that putting forward this proposal would not undermine our general stance on frontier controls in the single market, and might assist us to join in putting together an EC-wide system which would be more reliable than one of internal frontier preventive checks only. There is little doubt that any system of licensing and control which differs from the present one will increase the risk of diversion of licit supplies onto the black market but the trade is comparatively small and involves only a few well-known manufacturers who are and would remain subject to internal checks.

5. I recommend therefore that you support the Home Office proposal for the establishment of a working group of the Ad Hoc Group on Drug Addiction (on which Customs is represented) to examine what is a genuine problem. We do not anticipate rapid progress and we know that several other member states share our concerns. By the time the working group is ready to report, our line on remaining controls on MCAs, COCOM and other prohibitions and restrictions will be clearer. On the other hand, we should draw attention to the need for vigilance in the matter of Community competence and to the need to be careful not to weaken our overall line on frontier controls.

6. I attach a draft reply to the Home Secretary.

PS

P JEFFERSON SMITH

DRAFT

fix type final

INTRA-COMMUNITY FRONTIER CONTROLS

Thank you for your letter of 9 May asking whether I am content with a draft paper proposing the establishment of a sub-group of the EC Ad Hoc Working Group on Drug Addiction to consider the question of compliance with our obligations under the UN Conventions governing licit trade in narcotic drugs and psychotropic substances.

As you say, this has been the subject of discussion between my officials and yours, but I would ~~like~~ to draw your attention to two important points. First, we need to be vigilant in the matter of Community competence which, as you are well aware, could have implications for other aspects of UK policy. Second, we must be careful not to weaken our overall line on frontier controls.

Subject to these ^{two points,} ~~expressions of concern,~~ I am content for the paper to go forward as drafted.

A copy of this note goes to David Young.



P Jefferson Smith
Deputy Chairman

CHANCELLOR

Board Room
H M Customs and Excise
New King's Beam House
22 Upper Ground
London SE1 9PJ
Telephone: 01-382 5011

FROM: P JEFFERSON SMITH
DATE: 15 MAY 1989

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	Mr R I G Allen	
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	Mrs Chaplin	
	Mr Tyrie	

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5. I recommend therefore that you support the Home Office proposal for the establishment of a working group of the Ad Hoc Group on Drug Addiction (on which Customs is represented) to examine what is a genuine problem. We do not anticipate rapid progress and we know that several other member states share our concerns. By the time the working group is ready to report, our line on remaining controls on MCAs, COCOM and other prohibitions and restrictions will be clearer. On the other hand, we should draw attention to the need for vigilance in the matter of Community competence and to the need to be careful not to weaken our overall line on frontier controls.

6. I attach a draft reply to the Home Secretary.

PS

P JEFFERSON SMITH

DRAFT

INTRA-COMMUNITY FRONTIER CONTROLS

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Subject to these expressions of concern, I am content for the paper to go forward as drafted.

A copy of this note goes to David Young.

C.C. **PS/CHX2** PS/CSI,
PS/FST, PS/PMG,
MR SCHOLAR
MR. CULPIN,
MR. R.I.G. ALLEN
MR GILHOOLY
MR. MICHIE, MR CAU.
PS/Co E
MS. D. BARRETT,
MR JEFFERSON-SMITH
MR. J. TRACEY
MR. P. R. H. ALLEN
MR STEVENSON
MISS WEEKS
15 May 1989 MR. WILMOTT



Mrs Joan Davies
Chairman
Village Halls Forum
The Village Halls Office
The Old School
Cardington
BEDFORD MK44 3SX

Dear Mrs Davies

Thank you for your letter of 14 April, with which you enclosed a letter from Mrs Christiane Scrivener, the EC Commissioner, about VAT and village halls.

I am not convinced that Mrs Scrivener's letter can be read in quite as optimistic a light as you have done; it may be that all she means is that zero rating is permissible for village halls engaged in non-business activities (for example, if they accept donations from users rather than making set hire charges). As you know we would welcome a ruling which did not remove the benefits of zero rating from village halls. However, we could not introduce legislation to extend the interpretation of the Court's ruling beyond its apparent legal meaning without definitive guidance from the Commission. I have accordingly written to her to ask if the Commission can clarify precisely the circumstances in which zero rating is acceptable for village halls.

I shall write to you again as soon as I have a reply.

Yours sincerely
Peter Lilley
PETER LILLEY

Community Council of Devon

PMG 16 MAY 1989 - 1

County Hall
Exeter EX2 4QD
Telephone: (0392) 27



15 MAY 1989

ECONOMIC SECRETARY	
REC'D	16 MAY 1989
ACTION	Ms. D. Barnett
COPIES TO	PS/CHX, PS/FST PS/CST, PS/PMG
	MR. CULPIN, MR GILHOOLY,

President: Lt Col The Earl of Morley, JF

Director: Lt Col J. Leaver B.A.

Ref. V.5

12 May 1989

Mr Peter Brooke
House of Commons
LONDON

**URGENT
FOR IMMEDIATE
ATTENTION**

MR. MICHE, MR CALL
MR JEFFERSON - SMITH } C & E
MR WILMOTT

Dear Mr Brooke

On behalf of rural communities in Devon we ask you to please give special attention to the question of VAT which is being imposed on playing fields, community centres and village halls.

Our Euro MP, Lord O'Hagan maintains that it was not the intention of the European Court to impose VAT on charitable halls and other non-profit making community facilities. This is reinforced in a letter from Chrstiane Scrivener the new European Commissioner for taxation.

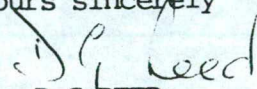
We have written to all Devon MPs on several occasions since the Court decision of 21 June 1988 and our hopes were raised that the Finance Bill might provide relief but the Draft Bill does not do so. Replies to our MPs from Mr Peter Lilley explained that Village Halls were businesses, a ruling with which no-one involved with halls in this County would agree. We hope that members of Standing Committee G will share our view for the following reasons:

There is no definition of business in the Customs and Excise Act 1983 and VAT legal advisers appear to rely on the decisions of two cases to determine that village halls are businesses. In our opinion it is wrong to reach a decision on cases not related to voluntary non-profit making charitable halls which provide social welfare facilities for village organisations eg: cubs, scouts, brownies, guides, elderly etc etc. We believe those cases have not been properly interpreted by HM Customs & Excise and hope your members will give full consideration to our views on this.

The Charity Commission insists that halls are Charities. Inland Revenue exempts them from tax and Rating Authorities from rates. Why does Customs & Excise insist they are businesses when it could easily and with more accuracy rule they are not? This is a nonsense.

Please support the amendments to clauses 17 and 20 proposed by William Powell MP when Standing Committee G discusses this on 16 May or exclude village halls and playing fields from the interpretation of the definition of business. Failure to act on this will result in hardship for many halls and small rural organisations run by volunteers, for whom there is no alternative provision.

Yours sincerely



D G REED
DEPUTY DIRECTOR

Registered Charity No: 200146



[Handwritten signature]

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

16 May 1989

Rt Hon Douglas Hurd CBE MP
Secretary of State
for the Home Department
Home Office
50 Queen Anne's Gate
LONDON
SW1H 9BW

cc PS/Economic Secretary
Sir P Middleton
Mr Wicks
Mr Lankester
Mr R I G Allen
Mrs M Brown
Ms Symes
Mrs Chaplin
Mr Tyrie

Mr Jefferson Smith - C&E
Mr Nash - C&E
Mr D Walton - C&E
PS/C&E

Dear Secretary of State

INTRA-COMMUNITY FRONTIER CONTROLS

Thank you for your letter of 9 May, asking whether I am content with a draft paper proposing the establishment of a sub-group of the EC Ad Hoc Working Group on Drug Addiction to consider the question of compliance with our obligations under the UN Conventions governing licit trade in narcotic drugs and psychotropic substances.

As you say, this has been the subject of discussion between my officials and yours, but I would draw your attention to two important points. First, we need to be vigilant in the matter of Community competence which, as you are well aware, could have implications for other aspects of UK policy. Second, we must be careful not to weaken our overall line on frontier controls.

Subject to these two points, I am content for the paper to go forward as drafted.

A copy of this note goes to David Young.

Yours sincerely

[Handwritten signature]

NIGEL LAWSON

[Approved by the Chancellor and signed on his behalf]



HM CUSTOMS AND EXCISE
CUSTOMS DIRECTORATE
DORSET HOUSE, STAMFORD STREET
LONDON SE1 9PS

Direct Dial 01-865 4777.....
Telephone 01-620 1313 Ext
GTN Number 3913

BROWN
→
PS/CX
7/6

PS/CHANCELLOR OF THE EXCHEQUER

From: MARTIN BROWN

Date: 7 JUNE 1989

OD(E) 8 JUNE : FRONTIER CONTROLS "BOTTOM LINE"

I attach briefs on papers

OD(E)(89) 11 : memo by Home Secretary

OD(E)(89) 12 : memo by Minister of Agriculture.

The briefs have been agreed with EC Division in the Treasury. IAE have not yet had a chance to see the papers and will advise any further points direct.

MARTIN BROWN
CD Division E

cc: PS Chief Secretary
PS Financial Secretary
PS Paymaster General
Mr Lankester
Mr R I G Allen
Mr Gilhooly
Mrs Brown
Mr Mortimer
Mr Bonney

Internal:

CPS
Mr Jefferson Smith
Mr Nash
Mr Wilmott
Mr Allen
Mr Cockerell
Mr Savins
Mr Walton
Mr Knox

FRONTIER CONTROLS : "THE BOTTOM LINE"

Papers : OD(E)(89) 11 and 12

*(these minutes missing, I'm afraid;
will keep chasing)*

Origin of papers

These two papers derive from the PM's request for a "bottom line" of the UK's minimum needs for frontier control of people and plant/animal health. The Home Office paper on people results from OD(E)'s last discussion of frontier issues on 13 April (OD(E)89 2nd meeting). The Foreign Secretary minuted the PM with our negotiating objectives and was asked for a clear statement of our minimum position. The MAFF paper on plant, etc health follows up earlier discussion in MISC 138 on 27 April with specific proposals.

Madrid European Council

In the light of discussion the Foreign Secretary is expected to advise the "bottom-line" positions to the PM before the Madrid European Council, where "frontiers" is a main agenda item. Following the Rhodes Council a national Co-ordinators Group has been looking into the frontier issues affecting movement of persons, identifying the areas where further work is still needed to permit frontier relaxation by 1993. The Madrid Council will consider the Group's report and the "bottom line" may be needed in argument. (A low-key discussion is looking likely, however: EMU and the Social Charter will provide enough scope for heated debate without stirring up frontier issues.)

Summary of Home Secretary's OD(E)(89) 11

Immigration needs: inspection of all passports to segregate non-EC;

: full examination of non-EC citizens (who in UK view have no Treaty rights of free movement)

Controls protect domestic labour market and social benefits from being

swamped by third country nationals. Alternative methods of control (compulsory ID cards, sanctions on employers) are more costly, less effective, unpopular. Dramatic extension of pre-entry visas undesirable, but hints at acceptability of Euro-visa, coupled with grant of leave to enter at internal frontier.

Terrorism needs: preservation of Special Branch's selective and random examination at UK ports and NI Land Boundary

Controls allow detention of suspected terrorists (Irish and international) and exclusion from UK of undesirables. Also gain valuable intelligence by observing and checking. Strengthening of EC's external borders would not trap Irish terrorists. Better EC information exchange could not replace intelligence gleaned at border.

Other crime needs: identify/observe/arrest wanted criminals

- : detect drugs smuggling (bulk quantities predominate at frontiers, large traffic intra-EC)
- : detect unlicensed firearms (EC proposals for Euro-licence for legal trade will not deter black market)
- : intercept serious pornography (much of it produced in EC where standards are far laxer than ours).

Summary of Minister of Agriculture's OD(E)(89) 12

Concern at the prospect of weakening the UK controls on animal, plant and fish health and food safety. Laxer standards could prejudice the favoured status of UK exports in some world markets, and also increase risks of compensation claims by farmers affected by outbreak of diseases. Paper proposes holding out for EC arrangements giving protection comparable to our existing (frontier-based) controls, including:

General: zones to be designated free of serious diseases and protected by checks at the boundary

- : right to take urgent national safeguard action at frontiers

: random frontier spot checks to supplement the internal control systems


: Commission power (and money) to make member states toe the line.

Animals: keeping quarantine arrangements

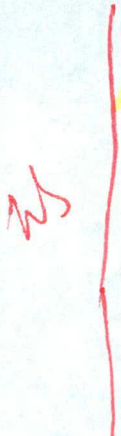
: frontier checks on travellers to detect rabid pets

Plants: "passport" for material certified free of disease

The paper notes that these objectives could be difficult to achieve under qualified majority voting, and points to the uncertain cost of the proposals (though likely to be less than the potentially adverse costs of laxer "inland" regimes).

 Line to take

You can support the Home Secretary's case that the essential interests of security and protection of society can be met most effectively and cheaply by maintaining frontier checks. Apart from the familiar 3rd country immigration, terrorism, drugs and firearms arguments, the paper raises the issue of pornography, where cultural attitudes in the EC (eg Denmark and Netherlands) vary markedly from the UK's.

 A further check on people not covered in Mr Hurd's paper is the probable need to retain limits on the amounts of alcohol and tobacco goods private travellers can import free of UK excise duty and VAT. The Commission's fiscal proposals are shifting, but still envisage no restrictions after 1992. This is unrealistic given the wide discrepancies in excise duties: the Co-ordinators' Group has noted it as an issue to be addressed. For health and revenue reasons, ceilings on travellers' allowances of tobacco and drink should be in the bottom line package, even though this means a residual fiscal frontier.

Other Ministers may raise a whole range of "lesser" prohibitions and restrictions currently enforced at import or export by Customs. Apart from

the animal/plant ones, there will need to be major political or tactical advantages to justify putting more items in the "bottom line" package.

The checks listed in Mr Hurd's paper are all justified by Article 36 of the Treaty of Rome, which recognised the right of member states to retain:

"..... prohibitions or restrictions on imports, exports or goods in transit justified on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants."

The Single European Act also carries a Declaration that:

"Nothing in these provisions shall affect the right of Member States to take such measures as they consider necessary for the purpose of controlling immigration from third countries, and to combat terrorism, crime, the traffic in drugs and illicit trading in works of art and antiques."

EC Division Treasury comments that the Home Secretary's recommendations leave room for judgement about the level and frequency of checks. It will be important to keep these to the minimum consistent with maintaining adequate control on immigration and crime, in order to:

- i). avoid undermining the single market objective of promoting (as far as possible) free movement of people and goods. Burdensome frontier checks do represent costs on business and the economy;
- ii). minimise public expenditure.

Treasury question whether it is essential to retain checks on outgoing passengers' passports (paragraph 2 of the paper), and whether full inspections are needed of incoming EC passports - rather than inspection of the covers only, with selective fuller checks. Treasury are not aware of costings which justify the statement in para 3 of the paper that a requirement for identity cards or passports to be carried by both British residents and overseas visitors would be more expensive and less effective than the checks proposed. They also point out that there are current proposals to relax considerably the conditions required for work permits for non-EC citizens.

The Minister of Agriculture's paper rightly argues for retention of existing border controls until suitably robust EC arrangements to provide comparable protection are agreed. The position in this area is more fluid, since EC proposals have yet to be made in many areas, and (as the paper hints) the credibility of "inland" controls will depend on the teeth of the powers and on the Commission's will to enforce them on laggard member states.

Removal of systematic border checks on veterinary and phytosanitary certificates will save (as yet unquantified) Customs resources and will contribute to faster throughput of freight traffic. Retention of quarantine, rabies checks on travellers, and spot checks for other plant, animal and food concerns are all sensible.

Points to make

On Mr Hurd's paper:

a) welcome the bottom lines proposed; consistent with Article 36 of Treaty and General Declaration in Single European Act;

b) particularly important to keep drugs in forefront of our armoury for retention of essential checks; Commission now coming round to our view (evidenced by Sir L Brittan's endorsement of checks at locations dictated by national circumstances);

c) on pornography, argue that without checks on internal border there would be no point in enforcing controls on third-country porn: resultant influx of hard-core paedophilia, bestiality and violent material;

d) advise likelihood of need to retain some (increased) limits on travellers' allowances of alcohol/tobacco on health and revenue grounds if - as seems likely - fiscal disparities remain too wide; and

e) are checks on outgoing passports really necessary? (At the most, such checks should be highly selective). Are full checks on incoming EC passports really necessary, rather than inspecting the covers only, with selective fuller checks?

On Mr McGregor's paper:

f) agree the need to remove systematic border checks in these areas: will contribute to true Single Market aim of speeding flow of trade (20%-30% of consignments are currently delayed for check of such paperwork);

g) query the dark hints of extra powers and resources for the Commission: will these be significant, and how funded?

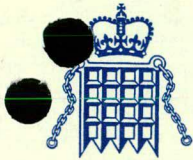
h) endorse the need to maintain the high standing of our agricultural exports (notably meat) in world markets; and

i) agree the UK's right to take emergency frontier action in any of these areas to protect national interests (covered by Article 36 of Treaty).

On both papers:

j) desirable to keep frontier checks to a minimum in order to promote 1992 objective of free movement (so far as possible) and to maintain downward pressure on public expenditure.

HM CUSTOMS AND EXCISE



HM CUSTOMS AND EXCISE
SINGLE MARKET UNIT
NEW KING'S BEAM HOUSE, 22 UPPER GROUND
LONDON SE1 9PJ
01-620 1313



Handwritten signature in red ink.

FROM: P R H ALLEN
Single Market Unit

DATE: 25 September 1989

CHANCELLOR

AD HOC GROUP ON FISCAL FRONTIERS: EXCISE DUTIES

The Ad Hoc Group held its first discussion on excise duties on 21/22 September. The meeting went much more positively than expected. A formal written report will not be provided for ECOFIN on 9 October, because discussions have, in one meeting, not advanced as far as those on VAT. However, we have been assured that M. Beregovoy, for the Presidency, will make an oral report to ECOFIN.

Circulation: Chief Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Mr Wicks
Mr Scholar
Mr Evans
Mr R I G Allen
Mr Culpin
Mrs M Brown
Mr Gilhooly
Mr White
Mr Michie
Mrs Chaplin
Mr Tyrie
CPS
Mr Jefferson Smith
Mrs Strachan
Mr Nash
Mr Wilmott
Ms Seammen
Mr Gaw
Mr Kent
Mr Savins
Mr Brown
Mr Pratt
Mr Knox
Mr Higgins
Mr Railton
Mr Mogg, Cabinet Office
Mr Arthur, FCO
Mr Norgrove UKREP

2. The main development to note is a very welcome one. We received much greater support than expected (from a majority of Member States, including the French) for the proposition which we pressed that a distinction needed to be drawn between "commercial" traffic and that involving private individuals crossing frontiers. This distinction would be based on giving greater freedom for such individuals to buy excise duty goods tax paid in another Member State subject to quantitative limits. This was considered as being part of the normal system and not by way of derogation. No mention was made of any commitments to non-divergence of excise duty rates. So far, so good.

3. Other salient points in the discussions were:-

(i) no discussion of duty rates or rate structures. The Commission are promising an early "working paper" on this, in advance of discussion of the full Commission on "flexible" rates, which would take account of Mme Scrivener's proposals at S'Agaro.

(ii) a majority of Member States (including the UK) favour a straight-forward system whereby goods not bought duty-paid by private individuals should move between Member States under a duty-suspension system between approved operators, e.g. bonded warehouses. This would be administratively the simplest system. However, some Member States and the Commission argued that to deny the possibility of commercial cross-border purchases of duty-paid goods would run counter to the intentions of the Single Market. Because of the administrative complexities and scope for evasion of this, we intend to continue to oppose it.

(iii) a number of Member States favoured rigid and fairly comprehensive systems to monitor cross-border (and even domestic) movements of excise goods. The UK, with wavering support from Netherlands, Ireland and Portugal, argued for a more liberal approach, with lower administrative and business compliance costs.

We may, however, need to agree compromises in this area, if we are to get agreement on a reasonably flexible arrangement on duty rates.

4. Overall, therefore, a quite encouraging start on excises, but there are a number of awkward hurdles ahead.

RA.

Richard Allen



FROM: J M G TAYLOR
DATE: 29 SEPTEMBER 1989

A handwritten signature in the top right corner of the page.

MR P R H ALLEN - C&E

cc PS/Chief Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Mr Wicks
Mr H P Evans
Mr R I G Allen
Mr Culpin
Mrs M Brown
Mr Gilhooly
Mr White
Mr Michie
Mrs Chaplin
Mr Tyrie

Mr Unwin - C&E
Mr Jefferson Smith -C&E
PS/C&E

AD HOC GROUP ON FISCAL FRONTIERS: EXCISE DUTIES

The Chancellor was grateful for your note of 25 September.

2. He has commented that he is impressed by the new logo on your notepaper!

A handwritten signature in the bottom right area of the page.

J M G TAYLOR

Central Statistical Office

Great George Street London SW1P 3AQ

Telephone 01-270 6040

Fax 01-270 5866

FROM: J E KIDGELL

BO581

5 October 1989

PS/CHANCELLOR

cc PS/Financial Secretary
Sir Peter Middleton
Sir Terry Burns
Mr Unwin
Mr Hibbert
Mr Nash
Mr Sedgwick
Mr Culpin

CHx

See questions at p. 21 of paper.
Skill I ask FST's views after
consulting Sir T B.

J

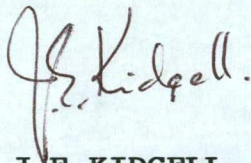
INTRA EC TRADE STATISTICS AFTER 1992

Ministerial responsibility for intra-EC trade statistics passed from DTI to Treasury on 31 July.

With the removal of most frontier controls after 1992, and the loss of Customs declarations a new system of collecting statistics of intra EC trade will need to be introduced. Representatives of the Commission and member states have been considering proposals for the replacement system for the past two years. The attached paper explains the background, the main issues and progress so far. In particular, it draws the Chancellor's attention to the close link between the basic VAT system and the collection of trade statistics, and the need for early decisions on the former before decisions can be taken on the latter.

The paper also seeks the Chancellor's agreement to officials' general approach to the issue of intra EC trade statistics.

The subject of trade statistics will be raised at the ECOFIN meeting on 9/10 October in the context of the Presidency Report of the Ad Hoc Fiscal group's deliberations on VAT. Briefing for this meeting has been prepared for the FST, taking account of the points raised in the attached note.



J E KIDGELL

Enc

INTRA-EC TRADE STATISTICS AFTER 1992

There will be a close link between the EC VAT systems and the collection of intra-EC trade statistics.

- (i) **Currently**, Customs' documentation is used to assemble trade statistics and to control the payment of VAT on imports. In the single market this documentation will continue only for trade with third countries.
- (ii) **After 1992**, in the single market, the replacement system for the collection of intra-EC trade statistics will depend crucially upon whether the EC VAT system is based on the origin principle, the destination principle, or a combination of the two.
 - a) if the origin principle, the system for collecting trade statistics would probably be largely independent of the VAT mechanisms, using them mainly to provide a register of traders and possibly as a useful cross-check;
 - b) if the destination principle, there could be an opportunity for joint reporting by traders for both VAT administration and trade statistics;
 - c) in the latest proposals on VAT by Commissioner Scrivener (mixed origin and destination principles), the collection of intra-EC trade statistics could be an integral part of the VAT system - the forms used for statistics being, in effect, tax returns.

So, the precise system for the collection of trade statistics depends on decisions taken on the VAT system, and must be agreed in the light of decisions on VAT.

2 Agreeing on and then implementing a new EC system of collecting intra-EC trade statistics will take a long time. If decisions on the basic VAT system are not taken in the very near future, a replacement statistical system may not be in place by 1.1.93. Officials believe that the time may already have passed to be sure of having all the details sorted out in time. In order to ensure that there is no break in the statistics officials feel that it is now prudent to make contingency plans for a UK system after 1992 in case the EC system is not in place by that date. This must not be allowed to divert too many resources from working on the new EC system, which might then be further delayed.

3 So early decisions on the basic VAT system are crucial for the smooth transition from the present system of collecting trade statistics to the agreed replacement system.

UK DECISIONS TAKEN

4 In the UK, Ministers have taken decisions on three issues:

- there is a continuing need for intra-EC trade statistics
- the EC statistical system should be controlled by a management committee where decisions are taken under qualified majority voting procedures
- the UK should press for classification nomenclature to be reduced to six digits.

5 The UK looked critically at its own future needs for these statistics. Ministers in the Chancellor's Departments agreed that there could be no question of discarding the intra-EC trade statistics altogether or of moving from monthly to quarterly periodicity. Data on foreign trade make up a significant part of the expenditure measure of GDP, and are essential for a comprehensive system of sectoral accounts. Ministers considered that it is vital prerequisite for efficient UK macro-economic management, especially in the short-term when recorded imports provide a particularly timely and accurate indicator of demand.

6 DTI Ministers decided that the new EC statistical system ought to be controlled by a management committee. This would give the UK power to negotiate on procedures to minimise official expenditure and unnecessary burdens on UK businesses which might result from excessive regulation by the Commission. The Commission is seeking to set up an advisory committee procedure where the committee provides an opinion which does not bind the Commission. The Commission has been proposing some very detailed implementing regulations. The Government decision was included in an explanatory memorandum on a Commission proposal submitted to Parliament by Francis Maude last March.

7 Ministers felt that savings could be made by reducing the classification to six digits for intra-EC trade. Treasury Ministers recommended this shift from the current nine digits. Six digits, they were advised, was the minimum level of detail required to produce an accurate split between prices and volumes in the aggregate figures. While a number of other Departments appear to have tacitly accepted the six digit proposition, MAFF Ministers continue to argue that an eight or nine digit classification is essential to the cost effective operation of the Common Agricultural Policy (CAP).

8 Most, if not all, other Member States now appear to be supporting the retention of the current eight digit nomenclature for intra-EC trade after 1992. Although the Commission originally preferred a simplified nomenclature it now seems likely that they may agree to the retention of eight digits. Sectors of UK industry maintain that cutting the nomenclature would have a minimal effect on compliance costs, but a cut to six digits would reduce running costs at Customs. Ministers may wish to reconsider the decision to seek a six digit nomenclature. If they do so, they may wish to take note of industry's views (see paragraph 12).

A NEW SYSTEM FOR TRADE STATISTICS - PROGRESS SO FAR

9 Since 1987, following the passing of the Single European Act and the tabling of the Commission's first proposals for tax harmonisation, Eurostat (the Statistical Office of the European Communities) has been consulting Member States on how trade statistics should be collected after 1992. They have been proceeding on the assumption that VAT will be based on the origin principle with a "clearing house" to reallocate the VAT to countries of consumption. A draft Council Regulation for a statistical system largely independent of VAT has been prepared; it was considered by the scrutiny committees of both Houses of Parliament in the Spring.

10 This Regulation would set the framework for the new system but would leave many details to be determined by later implementing legislation. INTRASTAT (the name of the new system) would collect information on intra-EC consignments from importers and exporters, but allows for collection to be undertaken in an aggregated form and periodically.

11 In discussions on INTRASTAT UK delegates have argued that it should be adapted to meet UK Ministers' basic objectives of the new system:

- it should be as cost effective as possible for Government (as collector) and business (as providers).
- it should only collect data needed for essential national purposes, and should not force the UK to collect additional (non-essential) data.

This second objective would be consistent with the Rayner principle that only data required for Government's purposes should be collected by Government, particularly if the information is collected under statutory powers.

12 Some parts of industry have expressed concern at the possible loss of detailed trade data after 1992 and have let DTI Ministers know of this concern. Before departing from DTI, the statisticians undertook, under Ministers' instructions, formal consultation with industry. Responses are still being assessed. Already two points are emerging on the controversial issue of the nomenclature. Responding businesses of all sizes argued that reducing the length of the code would have no effect on costs but would severely damage the usefulness of the data. They also argued strongly that the same commodity codes should be used both for intra-EC trade and for trade with third countries. A report to Treasury Ministers will be made in a few weeks.

FURTHER DECISIONS TO BE TAKEN

13 Final decisions cannot be taken until it is known what basic tax regime is planned. Little further progress can therefore be made on trade statistics. Officials believe that the draft framework legislation provides no more than a starting point. Amendments will be needed, and the UK can play an active role in the decision-making leading to subsequent implementing legislation. Official's view is that UK should seek to maximise the discretion left to Member States in the detailed setting up of the collection system.

14 Officials need ministerial agreement to this general approach and a steer on a number of more detailed points.

15 A key decision that will need to be taken is the Department responsible for collection. Officials' view is that H M Customs and Excise with its new and improved computer system (CHIEF) will be well placed to undertake this role most efficiently. Placing responsibility for the collection of both intra-EC and third country trade in one Department has obvious advantages. At some future stage, as decisions on the basic VAT system and then trade statistics emerge, Ministers will need to rule on this.

16 With the ending of the requirement to complete documentation before goods can be released for shipment, Ministers will need to consider what procedures for maintaining a high degree of compliance with the new trade statistics system should be introduced. This will, of course, have cost implications.

17 In the UK, 20% of traders account for just over 90% of the value of EC trade. Officials believe that costs and burdens should be kept to a minimum by seeking the most detailed monthly information only from this 20%, allowing the remaining smaller and medium sized businesses to make less frequent and much simplified returns. The accuracy of the overall trade data needed for macro-economic purposes should still be acceptable but the estimates for some individual products, traded predominantly by smaller traders, could be affected. This option would reduce running costs. Discussion has started in Europe and some support is emerging. However, if the Scrivener proposals on VAT were adopted the potential for seeking less information from small businesses would be lost.

18 Discussions about a new system for intra-EC trade statistics have so far been concerned only with the movement of goods. VAT is paid on many services traded between EC countries, and a logical extension of the fiscal proposals might be to treat statistics on taxable services in the same way as goods. UK officials have already raised this issue in EC meetings.

19 As explained in paragraphs 7 and 8, Ministers may wish to reconsider their position on the number of digits included in the nomenclature.

SUMMARY AND CONCLUSIONS

20 The Chancellor is asked to note:

- (a) the close link between VAT and trade statistics;
- (b) the need to take decisions on trade statistics in the light of those taken on the basic VAT system;
- (c) the need for early decisions to enable an agreed EC trade statistics system to be in place by 1.1.93^{or} as soon as possible thereafter; and
- (d) that, because agreement on the EC system has been delayed, officials are having to start formulating contingency plans to ensure the continued collection of intra-EC trade statistics in the UK after 1992.

21 The Chancellor's agreement is sought on officials' general approach to the new trade statistics system:

- to continue discussion in EC committees on the basis of the objectives outlined in paragraph 11;
- to aim for a system that minimises burdens on business and costs to Government, possibly by restricting collection of the most detailed monthly data to the largest 20% or so of intra-EC traders;
- to assume, for the time being, that Customs and its new CHIEF system will be the basis of the collection system;
- to consider further the possibility of including services within the same system as goods;
- to reconsider the number of digits included in the nomenclature.

In due course, as the options become clearer, Ministers will be presented with firmer proposals for decisions on these and other issues related to the collection of intra-EC trade statistics after 1992.

Central Statistical Office

5 October 1989



FROM: JOHN GIEVE
DATE: 6 OCTOBER 1989

PS/FINANCIAL SECRETARY

cc Sir P Middleton
Mr T Burns
Mr Sedgwick
Mr Culpin

PLP

Mr Unwin - C&E
Mr Nash - C&E

Mr Hibbert - CSO
Mr Kidgell - CSO

INTRA EC TRADE STATISTICS AFTER 1992

The Chancellor has seen Mr Kidgell's minute of 5 October. He would be grateful for the Financial Secretary's views.

Jc

JOHN GIEVE

UNCLASSIFIED

Ch. Content? 19/10



FROM: PAYMASTER GENERAL
DATE: 16 OCTOBER 1989

CHANCELLOR

SINGLE MARKET: EXCISE CONTROLS BY THE USE OF TAX STAMPS

You will be aware that, against the likely post-1992 background of significantly differing excise duties and no tax controls at frontiers, Customs have been researching the merits of tax stamps regimes for tobacco products and alcoholic beverages.

I have discussed the issues with officials and attach a synopsis of their findings, which are broadly that a system of tax stamps is both feasible and desirable for tobacco products, but has little attraction for controlling alcoholic beverages. I am inclined to agree that this should form the basis of the UK's response to new Commission excise proposals expected shortly which, it seems certain, will provide for tax stamp regimes.

The tobacco trade already applies tax stamps to product destined for some export markets, and, from Customs' informal contacts, expects to become subject to a similar regime post-1992. Fairly long lead-in times are entailed, however, and Customs are anxious to begin formal discussions with the tobacco trade and other interested parties on the detailed practical issues involved. In addition, Customs see opportunities for influencing the Commission on the essential features of any prospective tax stamp system and which could minimise costs to UK traders.

But there are features of the stamp systems which will need very careful watching: with some £5 billion revenue at stake from tobacco products alone, any adjustment to the duty deferment period could have some fairly significant Budgetary consequences; and I am concerned too about the prospect of having to give 6 to 8 weeks notice of future duty adjustments. I have asked Customs to see if there is some way around this.

It would be helpful to know if you endorse this general approach.

[Signature]
THE EARL OF CAITHNESS

TAX STAMPS

INTRODUCTION

Tax stamps are the prime method of revenue control for tobacco products in nine member states (UK, France and Ireland are the exceptions). Fewer use them to control alcoholic beverages. As the Commission is likely to propose stamp regimes post-1992, Customs have carried out detailed studies of systems operating in the EC and in the US. They conclude broadly that:

- a. tax stamps on all tobacco products would have substantial advantages for revenue collection and control; but
- b. for the control of alcoholic drinks, the disadvantages of any form of tax stamps outweigh the advantages.

TOBACCO

Systems

There are two general approaches. First, the tax stamp can be used to represent money (ie the manufacturer pays the tax appropriate to the product by buying the stamp, which is then placed on the package during the manufacturing process). In some countries the retail price is pre-printed on the stamp, which assists control. The tax stamps are security printed on high quality paper and accounted for accordingly. Second, the stamp can act simply as a marker, to show that the goods have been subject to revenue control. Tax collection would take place through a separate mechanism, probably much as now. The production and control of the stamps could be less rigorous. Customs think the first approach is right for the UK.

Trade Considerations

UK tobacco manufacturers already have some experience of tax stamps, being obliged to affix them to product destined for many

EC markets. Informal soundings suggest that the tobacco trade would accept, and even expect, a tax stamp system after 1992. There will, of course, be additional costs: equipment set-up and maintenance; funding the purchase of tax stamps; overprinting (possibly) and cutting; down-time when equipment fails; stamps destroyed beyond recognition; and accounting. Some of these costs, principally the funding of stamp purchases, could be alleviated by Government action. At present, the UK duty deferment system results in duty being paid at roughly the same time as the product is retailed. If stamps are to be purchased before manufacture, stretching the duty deferment period would avoid a cash flow disadvantage, either to manufacturers or to the revenue (provided Customs got the sums right). The trade would expect to benefit from protection of a market which would otherwise be threatened by undutied imports, from some measure of defence against parallel imports, and from deregulation (Customs controls could be lighter than at present).

Revenue Controls: benefits and costs

A tax stamp system pretty well polices itself. All products on the retailer's shelf must bear the appropriate authority's stamp. The stamp becomes such a feature of the product that its absence, or the sight of a 'foreign' stamp, should immediately arouse suspicion. Customs would no longer deploy staff at tobacco factories and could confine control to periodic brief visits to verify returned stock for duty credit purposes and to an annual audit of the trader's operations, which might be combined with VAT audit. The cost to the administration, assuming stamps were used as a tax collection device, would be in producing the tax stamps for manufacturers, who pay only the tax value represented by the stamp. Customs cannot yet accurately estimate the full cost, but expect it to be in the region of £1-2 million per annum.

Budgetary Issues

Overall revenues should not change under a tax stamp regime. However, it would probably be necessary to give 6 to 8 weeks'

notice of duty adjustments to allow the printers to produce tax stamps to the (revised) recommended retail prices chosen by manufacturers. However, forestalling by manufacturers - which is an annual problem for us under the present duty arrangements - would be less attractive under a tax stamping regime.

ALCOHOL

Systems

Studies in the EC and in the USA have convinced Customs that either as a means of tax collection or for controlling alcoholic beverages tax stamps have little to offer. The tobacco and drinks industries are structurally very different. Relatively few companies dominate the tobacco market, and distribution of finished product is straightforward. But the drinks market is broadly spread, with frequent distribution in bulk for bottling later. This leads to practical difficulties in applying tax stamps to drinks, with concomitant cost implications.

Different considerations apply to spirits, wines and beer:

- Beer is a comparatively low-tax product with high bulk. In draught form it does not lend itself to the application of stamps.
- Wine is our major imported alcoholic drink. However, because of the importance of wine to Community producers, the fragmented structure of the industry in the Community, and because it has such a low duty or is undutied in other Member States, there are grounds for doubting that a tax stamp system could work satisfactorily. Supplying duty-paid stamps to bottlers abroad would be logistically difficult; and even if stamps were only a protective device, the UK would have to depend heavily on the integrity of foreign administrative systems. The alternative - fixing stamps in the UK - is impractical. Neither wine nor beer is part of a tax-stamp system in any of the countries studied.

- Spirits are the only candidate for tax stamps and a feasible system could be established across the Community, although there are doubts about its utility, given the structure of the industry in the UK.

Trade views

Unlike tobacco goods (a small number of large producers familiar with tax stamps), bottled spirits present many problems. A greater proportion of spirits is imported than of tobacco products, and the industry is more fragmented (especially abroad), with wholesalers and distributors playing a greater role. The product can be stored and moved in bulk, unlike cigarettes. Duty collection through stamps therefore looks unattractive, though control could be enhanced. However, the Scotch Whisky Association (SWA) is strongly opposed to stamps and Customs know of no trade association that would favour them. Scotch whisky is the major drink in the Community (some £1.2 billion in value exported last year) and UK interests could be damaged by tax stamps. The main objections are on cost grounds. But stamps would also impose burdens on business and hamper an industry whose products are ill-suited to the re-packaging that would be a concomitant of a tax stamp system. As some 80 per cent of Scotch is exported, the burden on this sector of the industry would do little to assist UK control.

CONCLUSIONS

There is a strong case for a tax stamp system for collecting and controlling tobacco products duty after 1992. But on drinks the situation is more complex. Customs conclude that there is no national case for introducing tax stamps for drinks at all, and no Community case for putting stamps on beer and wine (it is either impractical or revenue risks are too low). If others were to make a case for using stamps for control of spirits (but not for duty collection), UK interests would be against it.



FROM: J M G TAYLOR
DATE: 17 OCTOBER 1989

A large, stylized handwritten signature in the top right corner of the page.

PS/PAYMASTER GENERAL

SINGLE MARKET: EXCISE CONTROLS BY THE USE OF TAX STAMPS

The Chancellor was grateful for the Paymaster General's note of 16 October.

2. He agrees with the Paymaster General's conclusions, ie that a system of tax stamps is both feasible and desirable for tobacco products, but has little attraction for controlling alcoholic beverages; and that this should form the basis of the UK's response to the new Commission proposals.

A smaller handwritten signature, likely of J M G Taylor, located below the main text.

J M G TAYLOR



FROM: FINANCIAL SECRETARY

DATE: 31 October 1989

CHANCELLOR ✓

cc

Sir P Middleton
Sir T Burns
Mr Sedgwick
Mr Culpin
Mr Owen
Ms Owen

Ch/ Essentially you need simply note Mr Kidgell's para 20 and agree to his para 21, subject to points made here by FST. you could ask Kidgell to take this work forward and keep FST (who has delegated responsibility for CSO) closely informed. DIS

Mr Unwin - C+E
Mr Nash - C+E
Mr Hibbert - CSO
Mr Kidgell - CSO

INTRA-EC TRADE STATISTICS AFTER 1992

Your predecessor asked for my comments on Mr Kidgell's submission of 5 October on intra-EC trade statistics after 1992.

2. CSO would like to continue negotiations with other member countries about a new statistical system on the basis that it:

- should be as cost effective as possible for Government and business
- should primarily collect data essential for government purposes.

There are also a number of detailed points, listed in paragraph 21 of Mr Kidgell's note.

3. In general I am content with the approach to the new trade statistics system described by Mr Kidgell. However, on the detailed points there are several issues which I think need clarification.

4. The costs and benefits of restricting the collection of the most detailed monthly data to the largest 20 per cent of traders needs more thorough investigation. In particular we need to be

sure that the macro-economic data will not suffer significantly. I note that Mr Kidgell says these series should still be "acceptable", but I think it would be useful to have a quantitative estimate of the potential reduction in accuracy of the macro statistics if only the largest 20 per cent of traders were to provide detailed information.

5. It would also be helpful to consider in more detail whether burdens on smaller traders would be significantly reduced if they were obliged to provide trade data at less frequent intervals than the larger traders. It may well be the case that the marginal costs of monthly provision compared to, say, quarterly provision are quite small. Finally, we would benefit from some quantification of the likely reduction in Government running costs from this option.

6. It seems sensible to assume for the time being that Customs should be the Department responsible for collecting the data. However, we will clearly need to consider this more carefully when decisions on the VAT system have been made.

7. The possibility of extending the system to cover trade in services is welcome. It could provide much more accurate data and it might be possible to provide a geographical analysis of trade in services. There are a number of questions that should be addressed:

- will third country trade be covered?
- what will be the additional cost of this extension?
- will we be able to dispense with any of the existing surveys used for collecting data on trade in services?

8. The original decision to argue for a reduction in the level of detail for intra-EC trade statistics was partly based on the assumption that this would allow significant savings to be made by industry (a six-digit nomenclature represents the minimum level of detail required for macro-economic purposes.) However, consultations with industry suggest that a reduction to 6 digits would be very unpopular. It is unlikely to reduce industrial

costs, and could even increase costs if industry decided it needed to collect the data itself. It is also now clear that the UK would be in a very small minority if it held out for the six-digit nomenclature. I therefore think it is now appropriate to review the original decision. But it is difficult to make an informed decision on this issue yet as there is no estimate of the cost savings to Government of a reduction to 6 digits.

9. I think we should ask CSO and Customs for an assessment of these cost savings, along with the full report they are preparing on the reactions of industry. Unless the cost savings can be shown to be sufficiently large, we should probably fall into line with other Member states on this issue.



PETER LILLEY



FROM: D I SPARKES
DATE: 8 NOVEMBER 1989

PS/FINANCIAL SECRETARY

cc Sir P Middleton
Sir T Burns
Mr Sedgwick
Mr Culpin
Mr Owen
Ms Owen

mp

Mr Unwin - C&E
Mr Nash - C&E
Mr Hibbert - CSO
Mr Kidgell - CSO

INTRA-EC TRADE STATISTICS AFTER 1992

The Chancellor was most grateful for the Financial Secretary's minute of 31 October commenting on Mr Kidgell's earlier submission. He would like Mr Kidgell to take this work forward under the supervision of the Financial Secretary and to take on board the Financial Secretary's comments.

D.I.

DUNCAN SPARKES