Report to the Council and the Commission on the realisation by stages of economic and monetary union in the Community (8 October 1970) — final version

Caption: On 8 October 1970, Pierre Werner, Luxembourg Minister of State, President of the Government and Finance Minister, submits to the Council of Ministers and the European Commission his final report on the conditions for the feasibility of an economic and monetary union.

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COUNCIL – COMMISSION
OF THE EUROPEAN COMMUNITIES

Report to the Council and the Commission on the realisation by stages of ECONOMIC AND MONETARY UNION in the Community

«Werner Report»

(definitive text)

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COUNCIL — COMMISSION

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Report to the Council and the Commission on the realization by stages of economic and monetary union in the Community

same as document 16.956/II/70-F, 8 October 1970

Luxembourg
8 October 1970

Summary

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FOREWORD

The present report completes the work of the group set up under Mr Pierre Werner, the Prime Minister and Minister of Finance of the Luxembourg Government, to look into the various aspects of the realization by stages of economic and monetary union in the Community.

In order to preserve unity in the presentation of the text it has been decided to combine in a single report the aspects that were considered in the interim report dated 20 May 1970 and those studied subsequently. Chapters I: introduction; II: starting point; and IV: the principles of realization of the plan by stages, have been taken to a large extent from the interim report. The same applies to chapter III: the final objective, except as regards the institutional reforms. On the other hand chapters V: the first stage; VI: the transition towards the final objective; and VII: conclusions, are almost completely new. Consequently, the present report contains an account of the whole of the work of the group.

I. INTRODUCTION

In accordance with the directives issued by the Conference of Heads of State or Government held at The Hague on 1 and 2 December 1969 and in accordance with the mandate given to it by a decision of the Council of Ministers of 6 March 1970, the Group, presided over by Mr Pierre Werner, the Prime Minister and Minister of Finance of the Luxembourg Government, presented to the Council of Ministers on 20 May 1970 an interim report on the realization by stages of economic and monetary union in the Community. In response to the invitation of the Council issued during its session of 8 and 9 June 1970 the Group has the honour to present its final report which completes and amplifies the interim report, in the light in particular of the directives that emerged from the exchange of views that took place in the course of the same session.[1] The present report does not reflect the individual preferences of the members of the Group but formulates replies in common. The ideas expressed are given on the personal responsibility of the members of the Group.

The formulation of the plan by stages presupposes that an examination will first be made of the present situation, facilitating a precise definition of the starting point and the development of a common concept of the state of economic and monetary union upon the completion of the plan by stages. Thus, having clarified the extreme limits of the development, the report sets out certain fundamental principles and specific proposals for starting and developing the process which should lead the Member States to economic and monetary union.

Without neglecting in any way the final phase of the process, the Group has thought fit to place particular emphasis on the first stage which implies concrete and important measures to be taken at the outset.

II. STARTING POINT

Since the signature of the Treaty of Rome, the European Economic Community has taken several steps of prime importance towards economic integration. The completion of the customs union and the definition of a common agricultural policy are the most significant landmarks.

1 cf. Annex 1. Communiqué from The Hague.
Annex 2: The Group's mandate.
Annex 3: Composition of the Group.
Annex 4: Decision of the Council of 8 and 9 June 1970.
Annex 5: Report transmitted by the Committee of Governors of the Central Banks of the EEC on questions put by the *ad hoc* Committee presided over by Mr Werner, and annexes.

However, the advances towards integration will have the result that general economic disequilibrium in the member countries will have direct and rapid repercussions on the global evolution of the Community. The experience of recent years has clearly shown that such disequilibrium is likely to compromise seriously the integration realized in the liberation of the movement of goods, services and capital. This is particularly true of the agricultural common market. Having regard to the marked differences existing between the member countries in the realization of the objectives of growth and stability, there is a grave danger of disequilibria arising if economic policy cannot be harmonized effectively.

The increasing interpenetration of the economies has entailed a weakening of autonomy for national economic policies. The control of economic policy has become all the more difficult because the loss of autonomy at the national level has not been compensated by the inauguration of Community policies. The inadequacies and disequilibrium that have occurred in the process of realization of the Common Market are thus thrown into relief.

The efforts expended have made it possible to achieve partial progress but they have not in fact led to the coordination or effective harmonization of economic policies in the Community, which would, however, have accorded with the spirit of the Treaty of Rome and which could have been realized to a large extent by the application of the fundamental provisions of the Treaty and in particular of the articles relating to economic and monetary policy.

Quantitative objectives sufficiently harmonized, which are one of the important conditions for effective coordination, have not been achieved in the first two medium-term programmes. Investigations that have been made into the economic situation in the Community have often not had any other result than recommendations formulated in altogether general terms, even when the Community interest calls for the assumption of a more positive position. In general, the consultation procedures have not yielded the results expected, either because they have been of a purely formal character or because the Member States have taken refuge in escape clauses.

The extension of the liberation of movements of capital and the realization of the right of establishment and of the free rendering of services by banking and financial undertakings have not progressed far enough. The delay has been caused by the absence of sufficient coordination of economic and monetary policies and by local peculiarities of law or of fact.

The freedom of persons to circulate is not yet assured in an entirely satisfactory manner and real progress has not yet been accomplished as regards the harmonization of social policies.

In the matter of regional policy, policies for particular sectors, and transport policy the progress realized has so far been fairly modest.

In foreign relations, and more particularly in international monetary relations, the Community has not succeeded in making its personality felt by the adoption of common positions, by reason as the case may be of divergencies of policy or of concept.

While these gaps have been appearing, economic agents have been adapting themselves at least partially to the new conditions in the markets. Thus, multinational companies have been formed and the markets in Euro-currencies and Euro-currency issues have sprung up and developed considerably. Furthermore, speculative movements of capital have assumed enormous proportions. These developments, some of which have positive aspects, help nonetheless to make still more difficult the control of economic development by Member States, while the constantly increasing interdependence of the industrialized economies throws into clearer and clearer relief the problem of the individuality of the Community.

The realization of the measures advocated in the memorandum of the Commission to the Council of 12 February 1969 may give a new impulse to the efforts of coordination and harmonization of economic and monetary policies. The realization of these measures, however, only provides a basis for the construction of the economic and monetary union which it is essential to conclude as soon as possible.

III. THE FINAL OBJECTIVE

The Group has not sought to construct an ideal system in the abstract. It has set out rather to determine the elements that are indispensable to the existence of a complete economic and monetary union. The union as it is described here represents the minimum that must be done, and is a stage in a dynamic evolution which the pressure of events and political will can model in a different way.

Economic and monetary union will make it possible to realize an area within which goods and services, people and capital will circulate freely and without competitive distortions, without thereby giving rise to structural or regional disequilibrium.

The implementation of such a union will effect a lasting improvement in welfare in the Community and will reinforce the contribution of the Community to economic and monetary equilibrium in the world. It presupposes the cooperation of the various economic and social groups so that by the combined effect of the market forces and the policies elaborated and consciously applied by the authorities responsible there may be achieved simultaneously satisfactory growth, a high level of employment, and stability. In addition, the Community policy should tend to reduce the regional and social disparities and ensure the protection of the environment.

A monetary union implies inside its boundaries the total and irreversible convertibility of currencies, the elimination of margins of fluctuation in exchange rates, the irrevocable fixing of parity rates and the complete liberation of movements of capital. It may be accompanied by the maintenance of national monetary symbols or the establishment of a sole Community currency. From the technical point of view the choice between these two solutions may seem immaterial, but considerations of a psychological and political nature militate in favour of the adoption of a sole currency which would confirm the irreversibility of the venture.

For such a union only the global balance of payments of the Community vis-à-vis the outside world is of any importance. Equilibrium within the Community would be realized at this stage in the same way as within a nation's frontiers, thanks to the mobility of the factors of production and financial transfers by the public and private sectors.

To ensure the cohesion of economic and monetary union, transfers of responsibility from the national to the Community plane will be essential. These transfers will be kept within the limits necessary for the effective operation of the Community and will concern essentially the whole body of policies determining the realization of general equilibrium. In addition, it will be necessary for the instruments of economic policy to be harmonized in the various sectors.

Quantitative objectives at medium term established in the form of projections compatible with one another and with the objects of the Common Market will be fixed at the Community level for growth, employment, prices and external equilibrium. These projections will be revised periodically.

Short-term economic policy will be decided in its broad outlines at a Community level. For this purpose to appreciate and fix the conditions of operation on global supply and demand, especially by means of monetary and budgetary policy, it will be necessary to establish normative and compatible economic budgets each year and to control their realization.

It is indispensable that the principal decisions in the matter of *monetary policy* should be centralized, whether it is a question of liquidity, rates of interest, intervention in the foreign exchange market, the management of the reserves or the fixing of foreign exchange parities vis-à-vis the outside world. The Community must have at its disposal a complete range of necessary instruments, the utilization of which, however, may be different from country to country within certain limits. In addition, it will be necessary to ensure a Community policy and Community representation in monetary and financial relations with third countries and international organizations of an economic, financial and monetary nature.

For influencing the general development of the economy *budget policy* assumes great importance. The Community budget will undoubtedly be more important at the beginning of the final stage than it is today, but its economic significance will still be weak compared with that of the national budgets, the harmonized management of which will be an essential feature of cohesion in the union.

The margins within which the main budget aggregates must be held both for the annual budget and the multi-year projections will be decided at the Community level, taking account of the economic situation and the particular structural features of each country. A fundamental element will be the determination of variations in the volume of budgets, the size of the balance and the methods of financing deficits or utilizing any surpluses. In order to be able to influence the short term economic trend rapidly and effectively it will be useful to have at the national level budgetary and fiscal instruments that can be handled in accordance with Community directives.

In this field, it is necessary to guard against excessive centralization. The transfers of power to the Community organs must be effected to the extent necessary for the proper functioning of the union, and must allow for a differentiated budgetary structure operating at several levels, Community, national, etc.

To make possible the abolition of fiscal frontiers while safeguarding the elasticity necessary for fiscal policy to be able to exercise its functions at the various levels a sufficient degree of *fiscal harmonization* will be effected, notably as regards the value-added tax, taxes likely to have an influence on the movement of capital and certain excise duties.

The suppression of the obstacles of various kinds should make it possible to arrive at a true *common market for capital* free from distortions. The financial policy of the Member States must be sufficiently unified to ensure the balanced operation of this market.

The realization of global economic equilibrium may be dangerously threatened by differences of structure. Cooperation between the partners in the Community in the matter of *structural and regional policies* will help to surmount these difficulties, just as it will make it possible to eliminate the distortions of competition. The solution of the big problems in this field will be facilitated by financial measures of compensation. In an economic and monetary union, structural and regional policies will not be exclusively a matter for national budgets. Furthermore, the problems of environment raised by industrial growth and urban development must be treated at the Community level under their various technical, financial and social aspects. Finally, the continuous development of intra-Community trade will find a new stimulus in a suitable transport policy.

The cohesion of the economic and monetary union will be the better safeguarded if the *social partners* are consulted prior to the formulation and the implementation of the Community policy. It is important to adopt procedures that confer on such consultations a systematic and continuous character. In this context, in order to avoid the emergence of excessive divergencies, the trend of incomes in the various member countries will be studied and discussed at the Community level with the participation of the social partners.

To resume, economic and monetary union implies the following principal consequences:

— the Community currencies will be assured of total and irreversible mutual convertibility free from fluctuations in rates and with immutable parity rates, or preferably they will be replaced by a sole Community currency;

— the creation of liquidity throughout the area and monetary and credit policy will be centralized;

— monetary policy in relation to the outside world will be within the jurisdiction of the Community;

— the policies of the Member States as regards the capital market will be unified;

— the essential features of the whole of the public budgets, and in particular variations in their volume, the size of balances and the methods of financing or utilizing them, will be decided at the Community level;

— regional and structural policies will no longer be exclusively within the jurisdiction of the member countries;

— a systematic and continuous consultation between the social partners will be ensured at the Community level.

A result of this is that on the plane of *institutional reforms* the realization of economic and monetary union demands the creation or the transformation of a certain number of Community organs to which powers until then exercised by the national authorities will have to be transferred. These transfers of responsibility represent a process of fundamental political significance which implies the progressive development of political cooperation. Economic and monetary union thus appears as a leaven for the development of political union, which in the long run it cannot do without.

The Group does not consider that it will have to formulate detailed proposals as to the institutional form to be given to the different Community organs; it nevertheless indicates the principal requirements to be observed by two organs that seem to it indispensable to the control of economic and monetary policy inside the union: a centre of decision for economic policy, and a Community system for the central banks.

The *centre of decision for economic policy* will exercise independently, in accordance with the Community interest, a decisive influence over the general economic policy of the Community. In view of the fact that the role of the Community budget as an economic instrument will be insufficient, the Community's centre of decision must be in a position to influence the national budgets, especially as regards the level and the direction of the balances and the methods for financing the deficits or utilizing the surpluses. In addition, changes in the parity of the sole currency or the whole of the national currencies will be within the competence of this centre. Finally, in order to ensure the necessary links with the general economic policy its responsibility will extend to other domains of economic and social policy which will have been transferred to the Community level. It is essential that the centre of decision for economic policy should be in a position to take rapid and effective decisions by methods to be specified, especially as regards the way in which the Member States will participate.

The transfer to the Community level of the powers exercised hitherto by national authorities will go hand-in-hand with the transfer of a corresponding Parliamentary responsibility from the national plane to that of the Community. The centre of decision of economic policy will be politically responsible to a European Parliament. The latter will have to be furnished with a status corresponding to the extension of the Community missions, not only from the point of view of the extent of its powers, but also having regard to the method of election of its members.

The constitution of the Community system for the central banks could be based on organisms of the type of the Federal Reserve System operating in the United States. This Community institution will be empowered to take decisions, according to the requirements of the economic situation, in the matter of internal monetary policy as regards liquidity, rates of interest, and the granting of loans to public and private sectors. In the field of external monetary policy, it will be empowered to intervene in the foreign exchange market and the management of the monetary reserves of the Community.

The transfer of powers to the Community level from the national centres of decision raises a certain number of political problems. In this respect it is fitting to quote in particular the relationship between the centre of decision for economic policy and the Community system of central banks as well as that between the Community organs and the national authorities. While safeguarding the responsibilities proper to each it will be necessary to guarantee that the Community organ competent for economic policy and that dealing with monetary problems are aiming at the same objectives.

A deeper study of the institutional problems thus raised is outside the framework of the mission of the Group, which has, however, thought it necessary to raise the essential aspects.

The implementation of economic and monetary union demands institutional reforms which presuppose a modification of the Treaties of Rome. Certainly, the present provisions already allow substantial progress to be made towards economic and monetary union, but a modification of the treaties will be necessary eventually to make possible a more advanced development of transfers of responsibility and the progressive establishment of the final institutions.

The Group considers that economic and monetary union is an objective realizable in the course of the present decade, provided the political will of the Member States to realize this objective, solemnly declared at the Conference at The Hague, is present.

IV. THE PRINCIPLES OF REALIZATION OF THE PLAN BY STAGES

In describing the desired result the Group intended to establish with clarity and precision the final objective aimed at. It is essential that there should be no misunderstanding in this matter, for economic and monetary unification is an irreversible process which must be approached with the firm intention to pursue it to its conclusion in the acceptance of all the implications contained in it on the economic and political plane.

The Group in no way wishes to suggest that economic and monetary union are realizable without transition. The union must, on the contrary, be developed progressively by the prolongation of the measures already taken for the reinforcement of the coordination of economic policies and monetary cooperation.

In every field the steps to be taken will be interdependent and will reinforce one another; in particular the development of monetary unification must be based on sufficient progress in the field of convergence and then in that of the unification of economic policies. Parallel to the limitation of the autonomy of the Member States in the matter of economic policy it will be necessary to develop corresponding powers at the Community level.

While pursuing its economic and monetary unification the Community will have to declare, vis-à-vis the outside world, its own objectives of international political economy. It is important that in adapting its internal structures it should continue to participate through the member countries or by itself in the measures for the liberation of trade, economic and monetary cooperation, and aid to developing countries that are decided on at the world level. Under these conditions, economic and monetary union will have served to reinforce the international division of labour and not to establish a new autarkic bloc within the world economy.

The Communiqué from The Hague envisages that the plan by stages for economic and monetary union will be formulated "on the basis of the memorandum presented by the Commission on 12 February 1969". The Group therefore considers that the actions advocated in the memorandum constitute the starting point for the whole process and that it is essential in consequence that the Council should pronounce before the end of 1970 on the only elements still outstanding in the memorandum, that is to say, on the one hand, the third medium-term programme setting out guidelines supported by figures and structural measures and, on the other hand, financial aid at medium term.

On the basis of these principles, the Group has first of all set out to clarify the principal measures to be considered in the course of the first stage for the purpose of reinforcing the common working practices of the national authorities and of providing the indispensable structures and mechanisms.

V. THE FIRST STAGE

The measures proposed for the first stage at once call for a substantial effort on the part of the Member States and the Community. It is necessary to guard against any excessive precipitateness, but the credibility and the smooth progress of the undertaking demand that a specific period should be fixed; the Group considers that a period of three years would be appropriate.

General arrangements

The reinforcement of the coordination of economic policies during the first stage seems one of the principal measures to be taken. One of the essential objectives to be attained will be to develop a rapid reciprocal exchange of information and to make possible the determination in common of the fundamental guidelines of economic and monetary policy.

A certain number of requirements and limits must be set. The coordination of economic policies necessarily entails constraint, but this can only be applied progressively. The arrangements to be adopted and the actions to be undertaken must aim at efficiency, and take account of the final concept of economic and monetary union. During the first stage the mechanisms and institutions necessary will be established and will function on the basis of the present provisions of the Treaty. However, the decisions taken must already be recorded in the progress of evolution that must end in the structure envisaged for the conclusion of the plan by stages.

Procedure

The coordination of the economic policies must be based on *at least three annual surveys* in depth of the economic situation in the Community that will make it possible to decide on guidelines in common.

The timetable indicated below has been deliberately left fairly flexible. Nevertheless, the surveys will be made on fixed dates. At the outset, these dates will be chosen in such a way as to ensure the best possible adaptation to the deadlines now in force in the Member States for the establishment and adoption of their budgets. Subsequently the deadlines will be synchronized so as to permit greater efficiency in the coordination of policies.

A *first survey* in the spring will provide an opportunity for drawing up a balance sheet for economic policy in the previous year and possibly for adapting that relating to the current year to the requirements of economic development. At the same time a first exchange of views will take place to prepare for the following meeting. In addition, the quantitative medium-term objectives will be revised according to the procedure laid down for drawing up the medium-term programmes of economic policy.

In order to arrive at the determination of quantitative guidelines for the principal elements of the whole of the public budgets for the following year and to enable governments to take note of the Community reactions before they draw up their budget plans, ordinary and extraordinary, on a definitive basis, a *second survey*, a little before the middle of the year will make an initial selection of the guidelines for the policy to be implemented in the following year and will review the policy to be followed during the current year. This analysis will be effected within the framework of the economic accounts and will make it possible to establish preliminary economic budgets.

Finally, a *survey carried out in the autumn* will make it possible to lay down in greater detail the guidelines arrived at in the course of the year. Economic budgets compatible with one another will then be drawn up. They will contain as regards budget policy the same elements as at the previous survey completed by additional data which would not have been available previously. The guidelines given in the economic budgets will serve as a point of reference for the authorities responsible for the determination of monetary and credit policy. On the occasion of this survey the Council will draw up, on the proposal of the Commission, an "*annual report on the economic situation of the Community*", indicating in particular the guidelines for economic policy at short term in the following year.

These regular examinations will make it possible to proceed to a permanent surveillance of the situation. However, as was foreseen also in the decision of the Council of 17 July 1969, *ad hoc* surveys may prove to be necessary for recommending or deciding on specific measures; they will be undertaken at the request of a Member State or of the Commission. In order to facilitate the detection of dangerous situations, a system of Community indicators will be worked out.

The recommendations regarding the guidelines for the economic policy to be followed will be addressed in a specific and detailed manner to each member country. Also, it is possible to envisage an arrangement of general import providing that in the event of such recommendations having to be put to the vote the country concerned would abstain.

The procedures for consultation will be reinforced by the abandonment of any previous obligatory restriction as to their character. These consultations will cover economic policy at medium term, short term economic policy, budget policy and monetary policy; they should lead to the formulation of national decisions in accordance with the points of view arrived at in common.

To ensure the necessary effectiveness, rapidity and discretion, special procedures must be envisaged for the preparation of the work, its development, and the conclusions. The procedures now in force are not adapted to the requirements of the case. The Group is fully conscious of the very heavy labours entailed in the proposed procedure. They demand great effort on the part of all the participants and assume that in both the Member States and the Community institutions the necessary conditions from the personal and organizational point of view will be fulfilled.

Organs

The coordination of economic policies during the first stage will depend on increased activity by the Community organs, in particular the Council and the Commission as well as the Committee of Governors of the central banks.

During the first stage the Council will be the central organ of decision for general economic policy. It will fix the objectives at medium term and within this framework will work out annual programmes. More generally, it will follow and direct economic policy throughout the year. In particular the Council will translate the intentions of general policy while defining the broad lines of budget policy.

The Council will be composed of the ministers responsible in each Member State for economic and financial matters, with the participation of the competent members of the Commission; the Governors of the central banks should attend the meetings. The meetings will be limited in number and will take place on the date fixed for the regular surveys mentioned above.

In order to ensure the effectiveness of the Council's labours on the basis of reports as up-to-date as possible and to guarantee a sufficient measure of coordination it must be possible to assemble rapidly persons of high standing representing Governments and central banks. These persons, who will thus not be sitting as independent experts, will have sufficient powers to facilitate the taking of decisions. Furthermore, they will be able to proceed to the consultations rendered obligatory by the decisions of the Council of 17 July 1969 and of 16 February 1970.

Important responsibilities will have to be assumed by the Commission, which will be entitled in particular within the framework of the powers laid down in the Treaties to make any proposal to the Council in order that the latter may rule on the matters in question. The Commission will make all necessary contacts with the competent national administrations, either direct or through Committees or groups of experts.

Greater activity will also be exercised by the different committees responsible for the problems of economic policy.

Finally, the Committee of Governors of the central banks will play an increasingly important role as regards problems of monetary policy both internal and external. The frequency of the meetings and the competence of the Committee will be adapted to ensure the preparation of the monetary aspects of the meetings of the Council envisaged above, to bring about current consultation and in particular to make it possible to define the general guidelines of monetary and credit policy within the Community.

The Committee of Governors will be able to express opinions or make recommendations to the central banks of the member countries when it wishes to give a particular direction to the action of the latter. It will be able to make recommendations to the Council and the Commission suggesting the Community measures that seem to it to be called for.

The proposals outlined above will help to ensure the coordination of economic policies, but it is advisable that at least once a year this should be the subject of a more formal approach. For this purpose the "annual report on the economic situation in the Community" brought out at the time of the survey scheduled for the autumn will be presented to the European Parliament and to the Economic and Social Committee, and the governments will bring it to the notice of the national parliaments for the latter to take into account in the debates on the budget proposals. An analogous procedure will be followed for the quantitative objectives at medium term determined at Community level.

"Concertation" with the social partners

For the successful realization of economic and monetary union it is essential to bring the social partners into the preparations for the Community economic policy. It is therefore necessary that major guidelines on economic policy should not be adopted until they have been consulted. For this purpose it will be necessary to establish at the outset procedures for regular "concertation" at the Community level between the Commission and the social partners.

Policies

Budget policy

Within the framework of the procedures already described special emphasis must be placed on the efforts to be made with a view to the coordination and harmonization of budget policies.

According to the economic situation in each country quantitative guidelines will be given on the principal elements of the public budgets, notably on global receipts and expenditure, the distribution of the latter between investment and consumption, and the direction and amount of the balance. Finally, special attention will be paid to the method of financing deficits or utilizing surpluses.

To facilitate the harmonization of budget policies, searching comparisons will be made of the budgets of the Member States from both quantitative and qualitative points of view. From the quantitative point of view the comparison will embrace the total of the public budgets, including local authorities and social security. It will be necessary to evaluate the whole of the fiscal pressure and the weight of public expenditure in the different countries of the Community and the effects that public receipts and expenditure have on global internal demand and on monetary stability. It will also be necessary to devise a method of calculation enabling an assessment to be made of the impulses that the whole of the public budgets impart to the economy.

From the practical point of view, it will be necessary to effect a harmonization of timetables for the presentation and adoption of the budget proposals.

Finally, from the very outset, efforts will be made to introduce and develop homologous instruments in each country; examples are, on the revenue side, the "fiscal regulators" and on the expenditure side, "cyclical budgets". Fiscal regulators authorize rapid adjustments in the rates of tax up to a limited amount and for a limited period; cyclical budgets permit the addition or reduction of final budget figures by a certain percentage of expenditure.

Fiscal policy

In order to permit the progressive and complete suppression of fiscal frontiers in the Community, while respecting the elasticity that is necessary in order that fiscal policy may have its effect at different levels, it will be necessary to realize in the various fiscal fields the measures enumerated below.

As regards indirect taxes, the system of the value-added tax will be made general and a programme for the alignment of rates adopted. Similarly, as regards excise duties, a programme leading to a sufficient alignment of the rates will be formulated for those that have a direct bearing on free movement across the frontiers.

The programmes of alignment will be carried out in a parallel manner and the rate of implementation will be such that as from the end of the first stage the controls on private individuals at intra-Community frontiers can be suppressed.

In the field of direct taxes, it will be necessary to standardize certain types of tax which are likely to have a direct influence on the movement of capital within the Community. In practice it is mainly a question of the harmonization of the fiscal regime applied to interest payments on fixed interest securities and dividends. It will also be necessary to initiate and actively promote the harmonization of the structure of taxes on corporations.

The policy for financial markets

The freedom of movement of capital within the Common Market has fallen short of the objectives fixed in the Treaty: in a certain number of countries there still exist exchange restrictions on important transactions; and in addition internal legislation and practices prevent the free circulation of capital within the Community. Disparities in the cost of credit and the conditions of access to credit resulting therefrom falsify competition and conflict with the institution of economic and monetary union.

To remedy this state of affairs, it seems necessary to take prompt action in two directions: the abolition of obstacles to capital movements, in particular residual exchange control regulations, and a coordination of policies as regards financial markets. This double action seems necessary so that the opening of markets can have its full effect and contribute to the smooth operation of the Common Market.

As regards the abolition of obstacles, it will be necessary as a first step to fix ceilings up to which issues of bonds by residents in other member countries may be authorized without discrimination resulting from exchange control regulations or administrative practices. These ceilings will be raised progressively until all the markets have been opened completely. Similar actions will be taken for the financing of investments by credit at medium and long term.

The introduction on the stock exchange of securities emanating from other member countries will be freed from all discrimination. In addition, it will be necessary to adapt the regulations governing institutional investors so as to enable them to effect placings throughout the Community.

As regards the coordination of policies in relation to financial markets a distinction must be made between current aspects and structural aspects. For the current aspects the member countries will proceed to regular consultations concerning the policy of equilibrium in the markets and the problems raised within and outside the Community by movements of capital; and they will initiate the concertation of national policies in these domains. As regards the structural aspect, it is necessary to carry out measures of "technical" harmonization in a series of fields, as for example regulations governing the activities of credit institutions and institutional investors, the notification and protection of holders of securities, conditions for the operation of stock exchanges, the encouragement of saving and certain forms of investment, and the legal instruments of financial transactions.

Domestic monetary and credit policy

The general lines of monetary and credit policy will be defined on a common basis. In this context it is necessary to introduce progressively a measure of conformity between the instruments of monetary and credit policy at the disposal of the member countries.

In order to ensure the coordination of domestic monetary and credit policies, prior obligatory consultations will be held within the Committee of Governors. These consultations will be effected in the following way : the Committee of Governors will examine periodically, and at least twice a year, the situation and policies in each member country in the monetary field. At the end of each scrutiny, and having regard to the conclusions arrived at by the Council for economic policy, guidelines will be laid down concerning the conduct of monetary and credit policy, principally as regards the level of interest rates, the evolution of bank liquidity and the granting of credit to the private and public sectors.

The measures to be taken should correspond to the guidelines formulated by the Committee of Governors and should be the subject of mutual reports prior to their application. If the competent authorities in one or several Member States, or the Commission, consider that the measures to be put into force are not in accordance with the guidelines given they may demand a consultation. In the event of dispositions departing from the guidelines given being contemplated by a Member State, the latter must arrange a consultation beforehand.

The harmonization of the instruments of monetary policy is one of the necessary conditions for ensuring the complete effectiveness of coordination and joint maintenance of the monetary policies. For this reason it will be necessary to establish without delay a programme for action in this field. In addition it is essential to press on with harmonization in order to ensure a better adaptation of the structures and statutes of the credit institutions to the requirements of a unified market.

External monetary policy

The process for the realization of economic and monetary union demands from the outset an intensification of cooperation in the matter of external monetary policy.

It is desirable that the solidarity of the member countries in the determination of their exchange parities should be supported by a reinforcement of the consultation procedures in the matter.

The reinforcement of concertation in the matter of monetary policy will concern the utilization and the granting of credits, as for example drawings from the International Monetary Fund and swap credits, the creation of new liquidity in the form of an increase in the quotas or a further development of Special Drawing Rights, as well as the foreign exchange position of the banks. It will be necessary to take a first step towards the progressive institution of a representative unit for the EEC at the IMF and other international financial undertakings.

In accordance with the decision of the Council of 8 and 9 June 1970, the Community must progressively adopt common positions in its monetary relations with third countries and international organizations; in particular it must not avail itself in foreign exchange relations between member countries of any provisions allowing greater flexibility in the international foreign exchange system.

As regards foreign exchange relations within the Community itself, the Group advocates for the first stage a certain number of measures the realization of which will be conditioned for each one by the result of the previous measure, so as to permit a constant adaptation of the process according to the circumstances:

— From the start of the first stage, by way of experiment, the central banks acting in concert will limit *de facto* the fluctuations in the rates of exchange between their currencies to narrower margins than those resulting from the application of the margins in force for the dollar at the time of the adoption of the system. This objective will be achieved by concerted action in relation to the dollar.

— After this experimental period the limitation of the margins can be officially announced.

— The concerted action in relation to the dollar can be completed by interventions in Community currencies, first at the limit of the margins and later within them. These interventions should be so arranged, however, that during the first stage the credit facilities to which they might give rise do not go beyond those provided for in the mechanism of monetary support at short term.

— Further reductions in the margins of fluctuation in the rates of exchange between Community currencies can be decided upon.

The first of the measures referred to above should be taken at the beginning of the first stage, when the Council will have adopted the plan for the realization of economic and monetary union; for the subsequent steps the Group thinks it better not to suggest a rigid timetable. For this reason it proposes that the Committee of Governors should twice a year make a report to the Council and to the Commission on the development of the measures being taken and on the advisability of adopting new measures. On this basis and according to the progress realized towards the harmonization of economic policies, the Council or the Member States assembled in the Council will take the appropriate decisions. Nevertheless, this procedure will not be necessary for reductions *de facto* in the intra-community margins resulting from the concerted action of the central banks.

In order to facilitate the development of the operations advocated it will be advisable to entrust to an agent the task of recording the balances of the operations effected in the foreign exchange markets of the member countries of the Community, to inform each central bank of them periodically and if the need arises to suggest transfers or possible offsets in Community currencies and in dollars.

It is necessary, finally, to undertake a study in depth of the conditions of creation and operation, and of the statutes of the "European Fund for monetary cooperation" outlined in chapter VI below and intended to ensure the necessary transition towards the Community system for central banks contemplated for the final phase.

The other fields

It is essential to pursue the measures undertaken in the various fields, for example the suppression of the residual obstacles to intra-community trade; an inventory of the aid and grants the standardization of which is necessary, on the one hand to ensure the free play of competition, and on the other hand to develop common industrial and regional policies; the formulation of a transport policy; the application of a common commercial policy in conformity with the Treaty; the implementation of a common policy in the matter of insurance and credit for exports and aid to countries in course of development; and the formulation and adoption of statutes for a European company.

The statistical apparatus of the Member States is still far from being satisfactory and presents gaps. To facilitate the coordination of economic policies it is essential that the efforts already made in this field should be renewed.

The institutional arrangements

In the course of this stage it will be necessary to complete the preparatory work designed to adapt and complete the Treaty, in order to permit, a sufficient interval before the end of the first stage and following the procedures laid down in Article 236 of the Treaty of Rome, the convocation in good time of an intergovernmental conference which will be apprised of the proposals formulated in the matter. In this way procedures will be adopted making it possible to establish the necessary legal bases for the transition to the complete realization of economic and monetary union and the implementation of the essential institutional reforms implied by the latter.

In the light of a balance sheet making it possible to measure the progress realized in all fields, the Council will then be in a position to establish a new programme of action containing measures that could be undertaken on the basis of the Treaty and others which would have to await its revision before they could be realized.

VI. THE TRANSITION TOWARDS THE FINAL OBJECTIVE

In the course of this final phase, action will have to be taken on a number of fronts. The action will entail, first further coordination of national policies, then their harmonization by the adoption of directives or common decisions, and finally the transfer of responsibility from the national authorities to Community authorities. As progress is made, Community instruments will be created to carry on or complete the action of the national instruments.

The coordination of economic and monetary policies will already have advanced to a point at which its fundamental elements are in place; subsequently it will have to be strengthened by ever closer regard for the common interest.

This will first have to be done in relation to *short-term economic policy*. To do this it will be necessary to isolate the conflicts and the lines of convergence in national policies. It will then be essential to define strategies aiming at the realization of a Community optimum which will not necessarily be a simple juxtaposition of national optimums. At the same time it will be necessary progressively to make the definition and general guidelines of economic policy more binding and ensure a sufficient degree of harmonization in monetary and budget policies.

The programmes of *economic policy at medium term* will have to be more and more closely geared to Community objectives, the realization of which will be ensured by policies conducted on the one hand at the national level and on the other hand at the Community level, the emphasis shifting gradually from the former to the latter.

In the matter of *budgetary policy*, the norms fixed for the variation in the volume, and for the direction and size of the balances on the public budgets, will be made increasingly restrictive. The homologous instruments of budget policy developed during the first stage will be applied progressively on a common basis.

The suppression of the obstacles of various kinds and the harmonization of the financial structures should make it possible to arrive at a true *common capital market* by the progressive interpenetration of the national markets.

In the framework of an economic and monetary union it is not enough to pay attention to policies of global economic equilibrium alone. It will also be necessary to envisage measures bearing on *structural problems* the essence of which will be profoundly modified by the realization of this process. In this context the Community measures should primarily concern regional policy and employment policy. Their realization would be facilitated by an increase in financial intervention effected at Community level. In addition, it will be necessary to arrive progressively at Community guidance for policies on industry, transport, power, housing, and the environment.

The reinforcement of intra-community links in the *monetary field* must be so formulated as to facilitate the transition to economic and monetary union, in which equilibrium between the economies of the Member States will be ensured by the free circulation of the factors of production and by financial transfers in the public and private sectors.

Progress in the convergence of economic and monetary policies should be such in the course of the second stage that the Member States no longer have to resort on an autonomous basis to the instrument of parity adjustment. In any case, it will be necessary further to reinforce the consultation procedures laid down for the first stage. Only at the moment of transition to the final stage will autonomous parity adjustments be totally excluded.

In order to prepare the final stage in good time, it will be necessary to set up as soon as possible a "European Fund for monetary cooperation" under the control of the Governors of the central banks. To the extent that the techniques of intervention in the foreign exchange markets laid down for the first stage and described on pages 22 and 23 have functioned normally and without friction and that sufficient harmonization has been achieved in economic policies it may well be possible to establish the fund in the course of the first stage. In any event it will have to be established during the second stage. This fund will have to absorb the mechanisms for monetary support at short term and for financial aid at medium term. As progress is achieved towards economic and monetary union the fund will gradually become an organ of management of the reserves at the Community level and be integrated at the final stage in the Community system of central banks which will then be set up. Furthermore, it will be necessary to bring about the harmonization of the instruments of monetary policy in order to facilitate the reinforcement of Community policy in this field.

VII. CONCLUSIONS

The Group, recalling that the Council adopted on 8 and 9 June 1970 the conclusions presented by the Group in its interim report, suggests to the Council that it should accept the contents of the present report and approve the following conclusions:

A. Economic and monetary union is an objective realizable in the course of the present decade provided only that the political will of the Member States to realize this objective, as solemnly declared at the Conference at The Hague, is present. The union will make it possible to ensure growth and stability within the Community and reinforce the contribution it can make to economic and monetary equilibrium in the world and make it a pillar of stability.

B. Economic and monetary union means that the principal decisions of economic policy will be taken at Community level and therefore that the necessary powers will be transferred from the national plane to the Community plane. These transfers of responsibility and the creation of the corresponding Community institutions represent a process of fundamental political significance which entails the progressive development of political cooperation. The economic and monetary union thus appears as a leaven for the development of political union which in the long run it will be unable to do without.

C. A monetary union implies, internally, the total and irreversible convertibility of currencies, the elimination of margins of fluctuation in rates of exhange, the irrevocable fixing of parity ratios and the total liberation of movements of capital. It may be accompanied by the maintenance of national monetary symbols, but considerations of a psychological and political order militate in favour of the adoption of a single currency which would guarantee the irreversibility of the undertaking.

D. On the institutional plane, in the final stage, two Community organs are indispensable: a centre of decision for economic policy and a Community system for the central banks. These institutions, while safeguarding their own responsibilities, must be furnished with effective powers of decision and must work together for the realization of the same objectives. The centre of economic decision will be politically responsible to a European Parliament.

E. Throughout the process, as progress is achieved Community instruments will be created to carry out or complete the action of the national instruments. In all fields the steps to be taken will be interdependent and will reinforce one another; in particular the development of monetary unification will have to be combined with parallel progress towards the harmonization and finally the unification of economic policies.

F. At this stage the laying down of a precise and rigid timetable for the whole of the plan by stages does not seem feasible. It is necessary in fact to maintain a measure of flexibility to permit any adaptations that the experience acquired during the first stage may suggest. Particular emphasis should therefore be placed on the first stage, for which a package of concrete measures is presented. The decisions on the details of the final stages and the future timetable will have to be taken at the end of the first stage.

G. The first stage will commence on 1 January 1971 and will cover a period of three years. In addition to the action approved by the Council in its decision of 8 and 9 June 1970 it will entail the adoption of the following measures:

1. The consultation procedures will have a preliminary and obligatory character and will call for increased activity by the Community organs, in particular the Council and the Commission, as well as the Committee of Governors of the central banks. These consultations will principally concern economic policy at medium term, short-term economic policy, budget policy and monetary policy.

2. The Council will meet at least three times a year to lay down, on the proposal of the Commission, the broad lines of economic policy at Community level and quantitative guidelines for the principal elements of the whole of the public budgets. Once a year, in the autumn, the economic policy in the Community will be the subject of recommendations contained in an annual report on the economic situation of the Community which will be transmitted to the European Parliament and to the Economic and Social Committee and which the Governments will bring to the notice of the national parliaments.

3. In order to promote efficiency in the Council's labours and to ensure sufficient coordination, the Council must be in a position to assemble rapidly persons of high standing representing Governments and central banks, who will be able to hold prior consultations.

4. Before the adoption of the broad lines of economic policy at the Community level, consultations will take place between the Commission and the social partners in accordance with procedures to be laid down.

5. The budget policy of the Member States will be conducted in accordance with Community objectives. For this purpose, within the framework of the meetings of the Council referred to in paragraph 2 above, a Community survey will be effected before the Governments draw up their budget proposals on a definitive basis. The national budget procedures will be synchronized. In the fiscal field, countries will adopt the harmonization advocated in the present report and the integration of financial markets will be intensified.

6. The Committee of Governors will play an increasingly important role in the coordination of monetary and credit policy; in particular it will lay down in this field the general guidelines for the Community. It will be able to express opinions and make recommendations to the central banks of the member countries and express opinions to the Council and the Commission.

7. To reinforce solidarity within the Community in the matter of foreign exchange, the central banks are invited, from the beginning of the first stage, to restrict on an experimental basis the fluctuations of rates between Community currencies within narrower bands than those resulting from the application of the margins in force in relation to the dollar. This objective would be achieved by concerted action in relation to the dollar. According to circumstances and to the results achieved in the standardization of economic policies new measures may be taken. These will consist of a transition from a *de facto* regime to a *de jure* regime of intervention in Community currencies and the progressive narrowing of the margins of fluctuation between Community currencies.

8. The actions foreseen in the foreign exchange field will be facilitated by the intervention of an agent charged with the tasks of statistical registration, information, and advice.

9. The rapid harmonization of the instruments of monetary policy is necessary. For this reason it will be necessary as soon as possible to undertake the preparatory work in this field.

10. The modifications to be made in the Treaty of Rome in order to make possible the final realization of economic and monetary union must be prepared in good time during the first stage.

11. In accordance with Article 236 of the Treaty of Rome, an intergovernmental conference will be called in good time before the end of the first stage with a view to drawing up the necessary modifications for the complete realization of economic and monetary union. A special meeting of the Council will be called to draw up a balance sheet of progress achieved in the first stage and lay down a programme for specific action in the years to come.

H. The *second stage* will be characterized by the promotion on a number of fronts and on ever more restrictive lines of the action undertaken during the first stage: the laying down of global economic guidelines, the coordination of short-term economic policies by monetary and credit measures, and budget and fiscal measures, the adoption of Community policies in the matter of structures, the integration of financial markets and the progressive elimination of exchange rate fluctuations between Community currencies.

The reinforcement of the intra-Community links in monetary matters must be effected as soon as possible by the establishment of a European Fund for monetary cooperation as a forerunner of the Community system of central banks for the final stage. In accordance with the experience acquired in the matter of the reduction of margins and the convergence of economic policies it may well be possible to establish the Fund during the first stage and in any event in the course of the second stage. The preparatory work for this purpose must be put in hand as soon as possible.

***

The Group expresses the wish that the Council should approve the suggestions contained in the present report and should make, on the proposal of the Commission, all the arrangements needed for the realization of the plan by stages, and in particular before the end of the year any that may be necessary to put the first stage into operation on 1 January 1971.

ANNEX 1

INTEGRAL TEXT OF THE FINAL COMMUNIQUÉ OF THE CONFERENCE OF THE HEADS OF STATE OR GOVERNMENT ON 1 AND 2 DECEMBER 1969 AT THE HAGUE

1. On the initiative of the Government of the French Republic and at the invitation of the Government of the Netherlands, the Heads of State or Government and the Ministers of Foreign Affairs of the Member States of the European Communities met at The Hague on 1 and 2 December 1969. On the second day, the Commission of the European Communities was invited to participate in the proceedings of the Conference.

2. Now that the final phase of the Common Market is about to begin they considered that it was the duty of those in each of the member countries of their Community who bear the heaviest political responsibilities to draw up a balance sheet of the work that has been achieved, to manifest their determination to carry it on, and to lay down broad guidelines for the future.

3. Assessing the ground covered, and observing that perhaps never before have independent States carried cooperation further, they were unanimous in the opinion that in view of the progress realized the Community has today reached a turning point in its history. Apart from the technical or legal aspects of the problems that it poses, the development scheduled for the end of the year is of major political significance. Entering into the final phase of the Common Market is not only in fact putting the seal on the irreversible character of the work accomplished by the Communities, it is also preparing the way for a united Europe capable of assuming its responsibilities in the world of tomorrow and of making a contribution corresponding to its tradition and its mission.

4. Consequently, the Heads of State or Government desire to reaffirm their faith in the political objects which give to the Community its whole meaning and significance, their determination to carry the enterprise through to its conclusion, and their confidence in the final success of their efforts. They hold in common the conviction that a Europe consisting of States which in their national diversity are united in their essential interests, assured of its own cohesion, faithful to its external friendships, conscious of the part it plays in facilitating the relaxation of international tensions and rapprochement between all peoples, and first and foremost between the peoples of the European continent

as a whole, is indispensable to the safeguarding of an exceptional cradle of development, progress and culture, to the equilibrium of the world and to the protection of peace.

The European Communities are the original nucleus from which European unity has developed and taken wing. The adhesion to these Communities of other countries in the continent — in accordance with the provisions of the Treaties of Rome — would undoubtedly contribute to the development of the Communities to dimensions approximating to an increasing extent to the present state of the economy and technology. The establishment of special links with other European countries who have expressed the desire for it should also play its part. Such a development would enable Europe to remain faithful to its traditions of opening up to the world and augmenting its efforts in favour of the countries in course of development.

5. As regards the culminating stage of the Communities the Heads of State or Government have reaffirmed the will of their Governments to pass from the period of transition to the definitive stage of the European Community and consequently to adopt the agricultural financial regulations at the end of 1969.

Within the framework of these financial regulations and taking account of all the interests involved, they agree to the progressive replacement of the contributions of the member countries by own resources with a view to arriving in the long run at the integral financing of the budgets of the Communities in accordance with the procedure laid down in Article 201 of the Treaty setting up the EEC and to reinforcing the budget powers of the European Parliament.

The problem of the method of direct elections will continue to be examined by the Council of Ministers.

6. They have asked the Governments to pursue without delay within the Council the efforts already undertaken to ensure a better control of the market by a policy of agricultural production making it possible to reduce budget charges.

7. The acceptance of a financial arrangement for the final period does not preclude its adaptation on a unanimous basis for the purpose in particular of enlarging the Community on condition that the principles of the arrangement are not altered.

8. They have reaffirmed their wish to carry on more rapidly with the further development necessary to reinforce the Community and its development into an economic union. They are of the opinion that the process of integration should end in a Community of stability and growth. With this object in view they have agreed that on the basis of the memorandum presented by the

Commission on 12 February 1969 and in close collaboration with the Commission a plan by stages should be drawn up by the Council during 1970 with a view to the creation of an economic and monetary union.

The development of monetary cooperation should be based on the harmonization of economic policies.

They have agreed that the possibility should be examined of setting up a European reserve fund, to which a common economic and monetary policy would lead.

9. As regards the technological activity of the Community, they have reaffirmed their wish to follow more closely the activity of the Community with a view to coordinating and encouraging industrial research and development in the key sectors, notably by Community programmes, and to furnishing the financial resources for the purpose.

10. They agree also on the necessity of making further efforts to formulate shortly for the European Atomic Energy Community a programme of research worked out according to the requirements of modern industrial management and calculated to ensure the most efficacious utilization of the Joint Research Centre.

11. They have reaffirmed their interest in the establishment of a European University.

12. The Heads of State or Government recognize the need for the reform of the Social Fund within the framework of a close concertation of social policies.

13. They have reaffirmed their agreement on the principle of enlargement of the Community as laid down in Article 237 of the Treaty of Rome.

In so far as States applying for membership accept the Treaties and their political objective, the decisions that have been taken since the entry into force of the Treaties and the options taken in the field of development, the Heads of State or Government have signified their agreement to the opening of negotiations between the Community on the one hand and applicant States on the other hand.

They have agreed that the preparatory work essential to the establishment of a basis of common negotiations may be undertaken at the most suitable and earliest opportunities; and these preparations will be accomplished by common consent in the most positive spirit.

14. As soon as negotiations with applicant countries have been opened, discussions will be started with the other member countries of EFTA who so request on their position in relation to the EEC.

15. They have called on the Ministers of Foreign Affairs to study the best way of realizing progress in the field of political unification with a view to enlargement. The Ministers will make proposals on this subject before the end of July 1970.

16. All the creative measures and measures for European growth here decided on will be assured of a greater future if youth is closely associated with them; this preoccupation has been borne in mind by the Government, and the Communities will proceed accordingly.

ANNEX 2

DECISION OF THE COUNCIL OF 6 MARCH 1970 REGARDING THE PROCEDURE IN THE MATTER OF ECONOMIC AND MONETARY COOPERATION

THE COUNCIL OF THE EUROPEAN COMMUNITIES

— with the object of giving effect at the first possible moment to the resolution on economic and monetary union in the Community passed by the Conference of Heads of State or Government held at The Hague on 1 and 2 December 1969 (paragraph 8 of the Communiqué),

— taking note of the suggestions formulated by the Governments and of the Communication from the Commission to the Council regarding the formulation of a plan by stages with a view to the creation of economic and monetary union,

DECIDES:

to invite the Chairmen of the Monetary Committee, of the Committee of Governors of the central banks, of the Medium-term Economic Policy Committee, of the Short-term Economy Policy Committee, and of the Budget Policy Committee, together with a representative of the Commission to meet under the chairmanship of Mr Pierre Werner to prepare a report containing an analysis of the different suggestions and making it possible to identify the basic issues for a realization by stages of economic and monetary union in the Community.

A first report will be presented to the Council and the Commission before the end of the month of May 1970, so that the Council can consider it.

Done in Brussels, 6 March 1970

For the Council

The President

ANNEX 3

COMPOSITION OF THE GROUP

	Deputies
Mr P. WERNER Prime Minister of Luxembourg	Mr J. SCHMITZ
Baron H. ANSIAUX Chairman of the Committee of Governors of Central Banks	Mr J. MERTENS de WILMARS
Mr G. BROUWERS Chairman of the Short-term Economic Policy Committee	Mr A. LOOIJEN
Mr B. CLAPPIER Chairman of the Monetary Committee	Mr J.-M. BLOCH-LAINE
Mr U. MOSCA Director-General for Economic and Financial Affairs in the Commission	Mr J.-C. MOREL
Mr J.-B. SCHÖLLHORN Chairman of the Medium-term Economic Policy Committee	Mr H. TIETMEYER
Mr G. STAMMATI Chairman of the Budget Policy Committee	Mr S. PALUMBO

Secretary: Mr G. MORELLI

ANNEX 4

EXTRACT FROM THE ABSTRACT OF DECISIONS 116th SESSION OF THE COUNCIL 8 AND 9 JUNE 1970

Statement by the Chairman, Mr Werner, on the proceedings regarding the plan by stages and the action to be taken on the interim report

The Council has endorsed the joint conclusions based on the proceedings of the Group presided over by Mr Werner, namely:

— the starting point of the process to be embarked upon is to be found in the completion of the measures advocated in the memorandum from the Commission to the Council of 12 February 1969. That implies that the Council will decide between now and the end of 1970 on the quantitative guidelines at medium term and the institution of financial aid at medium term;

— the final objective determined by the Conference of Heads of State or Government has emerged as an objective that may be reached in the course of the present decade, provided it enjoys the permanent political support of the Governments;

— economic and monetary union signifies that the principal decisions of economic policy will be taken at Community level and therefore that the necessary powers will be transferred from the national plane to the Community plane. Its final result could be the adoption of a sole currency that will guarantee the irreversibility of the undertaking;

— between the starting point and the achievement of the final objective numerous measures will have to be taken on a parallel and progressive basis on a number of fronts. Certain measures imply a modification of the Treaty of Rome the preparatory work for which must be brought to a successful conclusion during the first stage. Nevertheless, the present arrangements already allow substantial advances to be made;

— the first stage should commence on 1 January 1971 and be completed in a specified period; on the technical plane, a delay of three years seems appropriate. This stage will be intended to render the Community instruments increasingly operational and to confer individuality on the Community within the international monetary system;

— the first stage cannot be regarded as an objective in itself; it cannot be be dissociated from the entire process of economic and monetary integration. It must therefore be embarked on in the determination to arrive at the final objective;

— this first stage should include a reinforcement of the procedures for consultation according to methods which still remain to be determined; the budget policy of the Member States must be conducted in accordance with Community objectives; a certain harmonization should occur in the fiscal field; currency and credit policy must be strongly coordinated and the integration of financial markets must be intensified;

— the Community must progressively adopt common positions in monetary relations with third countries and international organizations; in particular it should not avail itself in the foreign exchange relations between member countries of any provision that would permit a weakening of the international foreign exchange system.

The Council has also invited the Group presided over by Mr Werner to continue its work in the light of the guidelines developed from the exchange of views that took place at the session of 8 and 9 June 1970 and paying due regard to any opinions of the Committee of Governors of the central banks that might be obtained on specific monetary problems. The Group is invited to present its final report in the month of September next.

ANNEX 5

COMMITTEE OF GOVERNORS OF THE CENTRAL BANKS OF THE MEMBER STATES OF THE EUROPEAN ECONOMIC COMMUNITY

The Chairman

Basle, 13 September 1970

Urgent and Confidential

Mr P. Werner
Prime Minister of the Government
and Minister of Finance
Luxembourg

Sir,

In your letter of 12 June 1970, you invited the Committee of Governors of the central banks of the Member States of the European Economic Community to give its opinion on certain technical and economic aspects of the proposals concerning progress in monetary matters contained in the interim report presented by the Group over which you preside.

The Committee of Governors has instructed a committee of experts to study the questions that you raised in your above-mentioned letter and which were then set out in a questionnaire drawn up by your Group at its meeting of 24 June 1970.

The Committee of experts whose work I have had the pleasure to direct has prepared a circumstantial report dated 1 August 1970 which I have the honour to send you herewith.

The Committee of Governors has examined this report; it considers that it answers the questions contained in your letter and in the questionnaire referred to above. It has adopted the conclusions arrived at, and in particular it considers that the inauguration of a foreign exchange regime peculiar to the Community might take as its starting point a concerted measure by the central banks calculated to restrict "in fact" fluctuations between their currencies within narrower margins than those resulting from the application of the margins in force for the dollar at the time the system is brought into effect.

Your obedient servant,

(a) H. Ansiaux

Committee of Governors
of the Central Banks
of the Member States
of the European Economic Community

Committee of Experts presided over by Baron Ansiaux

1 August 1970

REPORT ON QUESTIONS PUT BY THE COMMITTEE PRESIDED OVER BY Mr WERNER

Summary

I. Introduction

In accordance with the invitation of the Council of the European Communities the group presided over by Mr Pierre Werner, the Prime Minister and Minister of Finance of the Luxembourg Government, has asked the Committee of Governors of the Central Banks of the Member States of the European Economic Community for its opinion on certain specific monetary problems. This request has been the subject of a letter[1] dated 12 June 1970 from Mr Werner to Baron Ansiaux, the chairman of the Committee of Governors; the letter was subsequently dealt with in detail in a questionnaire[2] examined by the aforesaid group on the occasion of its meeting on 24 June 1970.

These two documents taken together contain the whole of the questions submitted for the opinion of the Committee of Governors on which the experts based their labours.

The Committee of Experts[3] took note of the fact that Question C in the above-mentioned letter, which concerns the actual tightening up of monetary policies and the harmonization of the instruments by means of which these are now controlled, should not be examined in detail having regard particularly to the delays entailed in the presentation of the opinion of the Governors. It nevertheless recognizes the fundamental importance of this question and suggests that the study of it should be undertaken as rapidly as possible.

The experts have examined the technical aspects of the problems with a view to preparing the answers that the Committee of Governors will have to give to the questions put to them. They have not sought to pronounce on the political expediency of the different courses that they have envisaged.

This technical examination has dealt essentially with the basic conditions, the methods, the consequences and the institutional procedures which, according to the terms of Mr Werner's letter, could ensue from the establishment of a specific system of foreign exchange for the currencies of the Member States.

II. Conditions to establish a specific system of foreign exchange

The specific requirements of the system of foreign exchange of the Community may be investigated in three principal directions, which in decreasing order of integration of the currencies are as follows:

(i) the establishment of a single Community currency;

[1] Cf. Annex 1.
[2] Cf. Annex 2.
[3] Cf. Annex 3.

(ii) linking the Community currencies to one another by parities and fixed rates;

(iii) differentiation between the margins of fluctuation allowed between Community currencies and the margins applied to the currencies of third countries.[1]

The experts consider that it would be premature to adopt formulae (i) and (ii) for the first step in the realization of economic and monetary union in the Community; and that they would be more appropriate to a later stage or even the final objective. They are unanimous in their view that in the course of the first phase the possibility represented by formula (iii) is the only one that should be envisaged.

The member countries of the Community having decided not to widen the margins of fluctuation in force between their currencies, the differentiation aimed at here can only take the form of a reduction or a suppression of the inter-community margins, or perhaps, in the event of a widening of the margins applicable to third currencies, of the maintenance, or the reduction, or the suppression of the inter-community margins.

III. Definitions

The "Community level" of the dollar will result from the common difference (fixed as a percentage positive or negative) allowed in relation to its parity as expressed in each of the Community currencies.

The rate for the dollar in each of the markets of the Community may deviate from this "Community level" by a percentage equal to half the amount of the fluctuations allowed for the Community currencies.

The range between the upper margin and the lower margin will be referred to hereafter as the "band"; it will fluctuate between the absolute limits applicable to the dollar according to the development in course of time of the "Community level".

These definitions are illustrated by the graphs shown below.

"Concertation" will have the object of fixing the "Community level" of the dollar whenever it may be necessary.

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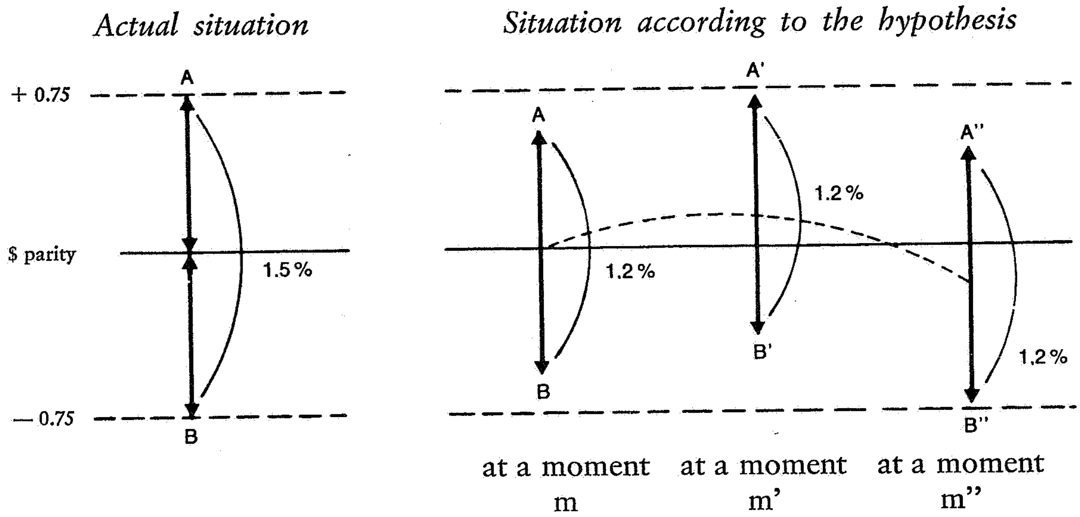
[1] The inter-community margins are at present different from the margins applied to the intervention currency, since these are established at about 0.75% each side of parity and the former at twice the margin applied to the intervention currency, or about 1.5% each side of parity. By "differentiation" is understood here the application to the intervention currency, that is to say the dollar, of an instantaneous margin of fluctuation narrower than the theoretical margin of ± 0.75% and at the most equal to half the agreed inter-community margin.

Hypothesis

— the margins of fluctuation applicable to the rate for the dollar remain fixed at 0.75% each side of parity.

— the margins of fluctuation applicable to the reciprocal rates for the Community currencies are reduced from 1.5% to 1.2% each side of parity between Community currencies.



A = Upper limit for dollar rate in the market in country A (currency A is weak).

B = Lower limit for dollar rate in the market in country B (currency B is strong).

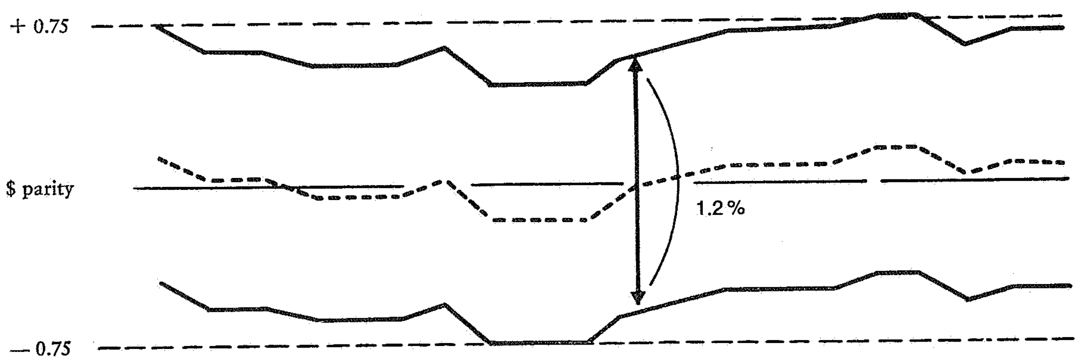
The dotted line (. . . .) represents the "Community level" for the dollar.

Consequences

The rate for currency A stands 1.5% below the parity expressed in currency B.

Situation on the basis of the hypothesis

Movement over a period



Consequences

The fluctuations of the dollar rate in the EEC markets are maintained within a "band" of 1.2% maximum, limited in the above graph by the external continuous lines; this "band" extends to 0.6% each side of a basic dollar level chosen in common (the "Community level").

The same type of graph would illustrate the other hypothesis of differentiation of the inter-community margins, that is to say of the maintenance or reduction of these margins, accompanied by a widening of the margin applicable to the dollar.

IV. Progressive reduction or outright suppression of the inter-community margins

(1) The experts of one central bank are of the opinion that the outright suppression of the inter-community margins, once the harmonization of the economic policies of the Member States has made sufficient progress, would have important advantages over a gradual elimination beginning at the first stage. In fact, in so far as the trends of balances of payments can still diverge the Member States have confliciting interests as regards the "Community level" of the dollar. These conflicting interests could lead to a situation in which it would not be possible to reach agreement on the intervention policy to be followed; under these conditions the experiment would come to an end. Even if a reduction in the margins were realized by means of informal concertation, it could not be done without the knowledge of the foreign exchange markets and a possible set-back to the experiment might then compromise the credibility of the policy of intervention and even confidence in the parity. On the other hand if agreement were reached in a situation of widely divergent balance of payments trends, the intervention rate agreed on might oblige one or several of the members to intervene against the natural trend of the market, which would be contrary to a sound logical policy. From the point of view of the monetary policy of the member countries, the narrowing of the margins would reduce their autonomy, and such a reduction is undesirable as long as autonomy on the economic and budgetary plane remains intact. Therefore the experts in question are of the opinion that any possible advantages of narrowing the margins from the outset are rather of a political and psychological nature and that these advantages raise certain doubts. They are not in particular convinced that a reduced autonomy on the monetary plane would necessarily lead to a greater degree of coordination of economic and budgetary policies in general, and they point out that a similar consequence was expected from the common agricultural market, it being hoped that this would eliminate adjustments in the parities of Community currencies. Certainly the narrowing of the margins would necessitate a reinforcement of cooperation between the central banks of the

Community, but cooperation in this field is destined to disappear in the final phase when the Community is furnished with a single currency, the external value of which will be maintained by centralized intervention.

(2) The majority of the experts consider on the other hand that on the hypothesis of a reduction in the margins of fluctuation between Community currencies, to narrow them progressively would be preferable to suppressing them without a transitional phase.

Certainly, on the purely technical plane the suppression of the margins without a transitional phase would present the advantage of requiring the central banks and the other participants in the foreign exchange markets to effect the necessary adjustments once and for all.

However, the immediate suppression of the margins would entail too severe a reduction in the autonomy of control of the Member States not only in their foreign exchange relations to one another but also in their foreign exchange relations with the outside world, which would then partake of a Community nature. It would raise the supposition that the necessary conditions existed on the economic and monetary plane to ensure the harmonization of economic policies and sufficient uniformity in rates of interest; it would also raise the supposition that unity had been achieved on the institutional plane in the management of the foreign exchange markets of the Community and in particular that a Community authority had been developed that was entitled to fix the level of the dollar.

For these reasons the suppression of the margins can only be contemplated at an advanced stage of the process of economic and monetary unification.

In the course of the development of this process, progress in the harmonization of economic policies would get the forces of the market moving in the direction of a progressive limitation of fluctuations in rates between Community currencies.

However that may be, to prepare the way from the outset, in accordance with the terms of the letter from Mr Werner, for a specific system of foreign exchange peculiar to the currencies of the Member States, it will only be possible to proceed by a progressive reduction in the inter-community margins or by widening the margins applied to the intervention currency, the inter-community margins being first of all maintained at their present level and then progressively reduced.

V. Methods of application of differentiation of margins

If account is taken of the fact that a reduction in the fluctuations in the rates between Community currencies can be effected either on an experimental basis and without a definitive undertaking, or in a more formal manner, three types of action can be envisaged for the introduction of a differentiation between the margins applicable to Community currencies and the margins applicable to third currencies.

1) Concerted action by the central banks of the Community in their foreign exchange markets with a view to *limiting in fact the fluctuations in rates between their currencies.*

On this hypothesis the inter-community margins would not be narrowed officially but the mechanisms necessary for the purpose would be established and brought into operation on an experimental basis.

2) *Official narrowing of the inter-community margins* to be determined in the light of circumstances.

In this case it would be for the Member States to work to a declared policy, the application of which would depend on the experience acquired under 1 above.

3) *Maintenance of the present inter-community margins and widening of the margins applicable to the dollar.*

This line of conduct could be adopted if, having regard to the situation and the policy in the United States, it seemed opportune to the six member countries of the EEC to widen the margins applied to the dollar either within the limits at present allowed or outside them if such a measure were to be authorized by the International Monetary Fund.

If a step in this direction were taken at the beginning of the process of economic and monetary unification it would render unnecessary the action described in 1 and could precede or accompany the phase described in 2.

Several advantages, at least in theory, attach to this latter type of action. In fact, the maintenance of the inter-community margins at their present level leaves intact the liberty of manœuvre of the monetary authorities of the member countries in their relations with the other members as regards the respective rates of exchange between the currencies of the Community, the level of interest rates and more generally the conduct of monetary policy.

Certain experts draw attention to the fact that the formula described in 3 might give the impression that the Community has chosen to adopt a policy of widening the margins of fluctuation. This formula, on the other hand, although it affirms the monetary individuality of the Community, would not at once lead the way to the suppression of inter-community margins which forms the final objective.

The respective consequences of the various formulae for the differentiation of inter-community margins in relation to the margins applicable to third currencies are examined in greater detail in Chapter VII below.

VI. Methods of intervention in the markets

Whichever type of action is adopted to obtain the desired differentiation, the same methods of intervention in the foreign exchange markets can be envisaged to obtain the desired result. The methods of intervention that help to limit the fluctuations in rates between Community currencies to a level that is independent of the margins applicable to the dollar fall into two categories:

1) Interventions in dollars exclusively, at "concerted" rates.

2) Combined interventions in dollars and in Community currencies.

(1) The fluctuations in rates between Community currencies may be limited to determined margins on condition that, by "concertation", the quotations for the dollar at a given moment are established in different markets in the Community in such a way that they are compatible with the margins adopted by the EEC countries for fluctuations between their currencies. The methods of achieving the necessary "concertation" are set out in Chapter VIII below.

The monetary authorities of each of the member countries would retain full liberty of manœuvre to intervene in dollars at rates within this band. Such interventions would become obligatory as soon as the quotations for the dollar reached the limits of the band, unless by "concertation" it was decided to shift this.

The possibility cannot be dismissed that in two or more markets in the Community the rate for the dollar might settle down at opposite limits of the band, and the reciprocal rate for the Community currencies concerned would thus reach the limit imposed by the inter-community margin. In these circumstances one central bank or even several might be obliged to intervene more rapidly at different rates from those that they would have adopted if they had been able to make full use of the whole of the margin applicable to the dollar. Any realignment of the band in one direction or the other would only alleviate the problems encountered by some central banks to the detriment of the central banks quoting the dollar at the other limit of the band. "Concertation" (cf. Chapter VIII) will then have to be resorted to to resolve such divergences of interest.

At a particular stage in the process of monetary integration "concertation" on interventions in dollars might be used as an instrument in the monetary policy of the Community vis-à-vis the outside world: in fact, it might be decided according to circumstances to vary upwards or downwards, over the whole margin applicable to the dollar, the rates for the dollar quoted in all the markets of the Community.

(2) Combined intervention in dollars and in Community currencies can be effected either at the limits of fluctuation of these currencies, limits determined by the new inter-community margins agreed, or within such limits. The technical problems are different in the two cases.

(i) In the first case the intervention is easier to realize than in the second, for the rates of intervention of EEC currencies will be known and fixed once and for all for any given inter-community margin; these rates might even be declared. The obligation to intervene at the limit points of the Community currencies would make such intervention automatic. It would, however, be fairly rare in view of the fact that the Community currencies ought not normally to be at a level corresponding to their maximum limits. As and when the Member States decide to reduce the maximum spread intervention in Community currencies at their limit would become more frequent.

(ii) Intervention in Community currencies within the limits of fluctuation for these currencies presupposes that the central banks maintain a permanent cooperation between themselves to ensure harmony in their intervention rates for Community currencies on the one hand and for dollars on the other. This harmony between the rates could be obtained by automatic application of cross rates. For that purpose it is essential that the central banks are informed at all times of the dollar rates quoted in all the markets of the Community and, of course, that the problem of "concertation" on the "Community level" of the dollar is settled. Moreover, intervention would only be effected with the agreement of the central banks whose currencies are being utilized.

(iii) In all cases, and as has already been said as regards intervention arranged in dollars, the central banks would retain their freedom to adjust the rate for the dollar inside the Community band.

By reason of its novelty and the adaptations it would necessitate, intervention in Community currencies could be introduced and developed on a gradual basis.

In the *first phase* the differentiation in the inter-community margins would be realized by means of concerted intervention in dollars exclusively.

A *second phase* would entail, apart from concerted intervention in dollars, intervention in Community currencies at the limits of fluctuation of such currencies.

Certain experts consider that a combination of the two first phases is technically possible. They see in it the advantage that the Member States would in this way affirm their intention to intervene at the limits of fluctuation of their currencies and would thus be able to loosen dependence on the usual intervention currency, that is to say the dollar.

Other experts think however that for both technical and tactical reasons it would be better to acquire experience and establish the proper functioning of intervention in dollars as provided for in the first phase before undertaking intervention in Community currencies at the limits of the margins. It appears to them in fact that concerted intervention against the dollar is at least as effective as other methods of intervention and that it can lead equally well to the individualization of the currencies of the Community by a progressive elimination of the margins of fluctuation between these currencies.

It is possible that in a *third phase* intervention in Community currencies could take place within the limits of fluctuation of these currencies, at rates determined by the cross rates, and on the lines which have been described above. Some experts consider that for the purpose of attaining the end in view it would not even be necessary to adopt such a method, with the technical complications that they see in it.

Whatever the more or less rapid course chosen for intervention in Community currencies the central banks could seize every opportunity that presented itself for effecting it, step by step or on an experimental basis. The foreign exchange markets would in this way become accustomed progressively to intervention in Community currencies.

VII. Consequences of differentiation in inter-Community margins

The differentiation of inter-Community margins could have repercussions on the reserves, the relations between rates of interest and the interest-rate policy of Member States, forward rates of exchange and the application of agricultural policy. As has already been indicated in Chapter V of the present document these repercussions may vary, according to the formula adopted.

1) Reserves

(i) *Reserve requirements*

A differentiation realized by a *formal reduction or a de facto reduction in the inter-Community margins* could lead the central banks to intervene more frequently in their foreign exchange markets by reason of the fact that with more limited possibilities of fluctuation for the Community currencies intervention could take place earlier than before. Nothing proves on the other hand that this shift in the time and the point of intervention would have a marked net effect as regards either gains or losses on the volume of the reserves of the central banks. In fact, the foreign exchange markets would to a large extent continue to ensure the necessary compensation. Furthermore, the limitation of the possibilities for fluctuation in the rates of Community currencies might dispose the commercial banks to hold those currencies more willingly. This process would normally gather strength in proportion to the narrowing of the inter-Community margins.

In any event if the narrowing is slight there is reason to think that the reserve requirements would not be modified to any extent, since they correspond essentially to the trend of the balance of payments.

On the hypothesis that the differentiation in the inter-Community margins would be realized by means of combined intervention in dollars and in *Community currencies*, a saving of reserves could be achieved to the extent that the balances in Community currencies are not subject to daily settlement in other means of reserve. The central banks would thus have relatively more dollars at their disposal for operations with third countries.

It is to be noted on the one hand that intervention in Community currencies and the retention of these in the reserves of Member States would leave unchanged the total amount of assets held in other forms by the Community as a whole; and on the other hand that at a more advanced stage, when there are no longer margins of fluctuation between Community currencies, third countries might be tempted to hold them. This could only develop if in addition changes of parity were precluded as between Community currencies and if at the same time satisfactory investment outlets were provided for them.

In the event of a differentiation in the inter-Community margins obtained by means of a *widening of the margin applicable to the dollar*, the movements in the reserves might become less important, given that the Member States would be in better position to protect themselves by variations in the rates against inflows or outflows of dollars.

Examination of the consequences on the reserve requirements of a differentiation in the inter-Community margins leads to the conclusion that the adoption of differentiation will not necessarily entail the provision of specific credit facilities.

(ii) *Nature and management of the reserves*

The repercussions in this field will depend very largely on the methods of intervention adopted by the central banks to obtain a differentiation in the inter-Community margins. Concerted action against the dollar alone will bring no changes in relation to the present situation; and it will be the same if concerted intervention is similarly effected against Community currencies but does not lead to holding them in the official reserves of the Member States.

Conversely, if they are so held, the central banks will have to consider the following questions:

— limits on the holding of Community currencies in the official reserves;

— exchange guarantees relative to such holdings (these could easily be arranged on a swap basis, under the provisions of the European Monetary Agreement, or by holding them in the form of units of account);

— return on the reserves in Community currencies by comparison with those held in dollars, in the form of special drawing rights, or in the form of claims on the International Monetary Fund.

Altogether, the influences of a reduction in the inter-Community margins on the nature and the management of the reserves should not be a difficulty. It would even carry advantages to the extent that the retention of Community currencies in the reserves of Member States would seem preferable to other assets.

2) Rates of interest and forward rates of exchange

The examination of the repercussions of a differentiation in inter-Community margins is made on a hypothesis that ignores particular tensions due to doubts about the parities of certain Community currencies. Such doubts generally provoke speculative movements of capital, unpredictable and substantial, on which the width of the margin has practically no influence.

In principle, narrowing the inter-Community margins should reduce the need for forward cover between the currencies of the Member States.[1] Subject to forward cover arrangements intended to guard against the risk of changes in parity, still not perhaps totally excluded within the Community, these needs will diminish in proportion as the margins are narrowed, and will finally disappear.

The reduction in the need for forward cover will tend to narrow the differences between rates of interest in force in the Member States and thus reduce the autonomy of national policies in this domain. It is to be noted on the other hand that a widening of the margins for the dollar will increase the need for forward cover in third currencies and the possible extent of the differences between the rates of interest in the markets of third currencies, especially the Eurodollar market, and the rates ruling in the markets of the EEC countries.

In consequence, a reduction in the inter-Community margins would provide an incentive to greater uniformity in monetary policies inside the Community; while a widening of the margins for the dollar would provide greater autonomy and greater liberty of manœuvre in relation to other countries.

1 The reduction in the need for forward cover might be less in the event of a *de facto* narrowing than an official one, since in the former case the economic agents operating in the foreign exchange markets would not know the new limits set for the fluctuations in rates of Community currencies.

Apart from these advantages, the experts have recognized, however, that a reduction in differences in rates of interest inside the Community might present difficulties. In fact, seeing that uniformity in national economic policies is not sufficiently assured, that interest rate policies vary in importance in different member countries, and that the systems of financial relations with foreign countries vary widely within the EEC, undesirable movements of capital could occur, and to deal with them the Member States would be progressively deprived of possibilities of action by the interplay of fluctuations in rates, and they would then have to apply other measures.

The existence of these difficulties or dangers has led the majority of experts to put the accent on the expediency of a progressive narrowing of inter-Community margins, having regard, among other things, to the fact that a slight reduction in the margins still leaves the possibility of important differences of interest rates between Member States.[1] On the other hand, the experts are unanimous regarding the necessity for undertaking a study of methods making it possible to harmonize monetary policies and the utilization of the instruments of such policies, in order to avoid recourse to measures of control conflicting with the smooth running of the Common Market.

3) Common agricultural policy

In restricting the possibilities of fluctuation in rates of Community currencies for spot settlement and in consequence for forward operations, the reduction in the inter-Community margins could have a beneficial effect on the application of the common agricultural policy, notably as regards divergent movements for products caused by slight differences in rates.

The experts, however, are not all convinced that such a favourable consequence would follow. They consider that in essence the problems of agricultural exchanges are bound up with other factors than the margins of fluctuation of currency rates, in particular with institutional elements and the variations in forward exchange rates that may occur in a period of speculation. However that may be, a reduction in the inter-Community margins cannot have any harmful effects on the common agricultural policy.

VIII. Institutional arrangements for "concertation"

A. Operation

When the decision has been taken to differentiate between the Community margins and those applicable to the dollar, "concertation" aimed at

[1] On the hypothesis that inter-community margins are reduced to ± 1% (instead of ± 1.5%) the difference between the levels of interest rates in force in the member countries for operations at three months would amount at the maximum to 8% per annum.

determining the spread of the inter-Community margins and at fixing for the first time the "Community level" of the dollar should be effected between the Governors of the central banks of the Member States. In fact, such "concertation" would be a determining factor for future developments; and it is important that it should be carefully prepared.

It would be desirable that at the moment when it is decided to put the system into operation the rate for the dollar in terms of each of the Community currencies is well within the "band" selected.

Once this first decision has been taken the "concertation" can be continued either between the central banks direct or within a Community organ.

B. Direct "concertation" between central banks

1. Such "concertation" should be constant. It could take the form of daily contacts between those responsible for the conduct of the foreign operations of the central banks, and it would be for them to maintain the necessary contact with their authorities.

2. The Committee of Governors, informed of the development of the situation in the foreign exchange markets of the Community, would lay down at their meetings the broad lines of the policy of intervention to be followed. These would serve as a guide for the decisions to be taken from day to day by those responsible for the conduct of the foreign operations.

3. The experts recognize unanimously that no grave problem should normally arise as long as the rates for the dollar in the different markets of the Community remain inside the "band".

4. Certain problems might arise:

(i) If the rate for the dollar vis-à-vis a Community currency moved to the upper or lower limit of the "band" and the central bank issuing the currency concerned desired to shift the "Community level" in order to secure greater freedom of fluctuation while other central banks preferred not to modify it.

(ii) If the rate for the dollar against two or more currencies of the Community were at opposite limits of the "band" and one central bank wished to raise the "Community level" while another wanted to lower it.

On the former hypothesis the "concertation" body would have to decide whether there was a case or not for shifting the "Community level" and fix the amount of such movement. In the second case, it would have to come to a decision as to the wisdom of the movement and on the amount and direction of the movement to be made at that level.

5. In order to avoid as far as possible being taken by surprise it would be best if "concertation" were effected as soon as the rate for the dollar in relation to a Community currency approached too closely one of the limits of the "band" (within 0.10% for example).

This would provide a breathing space during which the necessary contacts could be made.

6. In any event, if "concertation" at the level of those responsible for the conduct of the foreign operations did not result rapidly in a decision, the Governors would be immediately apprised of the situation and — whether they were to meet or to consult by other methods — they would have to decide on a solution of the problem submitted to them.

The "concertation" at whatever level it takes place must always be multilateral, even if certain central banks appear not to have any direct interest in the case in point, for the fixing of the "Community level", determining as it does the position of the "band", is a question of common interest.

7. At the "concertation" all the elements of fact likely to exercise an influence should be taken into consideration (level of reserves, duration of disequilibrium noted, seasonal influences, etc.).

Among these elements there are two in particular that deserve special attention.

The first is the percentage accumulation or loss of reserves sustained by the country desiring a change in the "Community level". In fact, the amount of these movements could provide an indication of the size and direction of the change to be made in the "Community level".

The second is the amount and direction of the net global position in the aggregate of the five central banks of the Community in relation to the outside world.

This indication should make it possible to judge the interests of the Community in relation to those of any one of its members.

Community actions — such as recourse to the support of a currency at short term — might eventually be contemplated to make up for the difficulties entailed for certain central banks in the compromises accepted by them in the interests of the Community.

8. Independently of the cases considered above in which it might be necessary to change the "Community level" there may well be others in which the central banks decide by common accord to act on the dollar rate either by raising it or lowering it deliberately in response, for example, to the exigencies of monetary policy.

Such action would also require "concertation", which would normally be held at Governor level.

9. Finally, it seems necessary to undertake rapidly a study of certain problems of a material and technical nature, of which the following are singled out for mention in the first place:

(i) establishment of a communications network permitting direct, immediate and simultaneous contact between central banks;

(ii) unification of the methods of intervention in foreign exchange markets;

(iii) standardization of the opening hours of the markets.

C. Concertation through the intermediary of a Community organ

1) *Object*

1. The methods described above enable the central banks to reduce progressively and then to suppress the margins of fluctuation between Community currencies, but they do not lead by themselves to the wider objectives required of an economic and monetary union which the Heads of State or Government decided to establish at the Hague Conference.

2. In fact the narrowing of the margins, concerted intervention against the dollar, and any intervention in Community currencies only go some way towards ensuring the "Community management" of the operations of the central banks.

Now, at the final stage of the economic and monetary union the necessity has been accepted:

— not only to eliminate the margins of fluctuation between Community currencies,

— but also to pool and manage in common the foreign exchange reserves of the Community

— and in addition to establish a Community authority, analogous to the Federal Reserve Board, entitled to take decisions of monetary policy in the matter of discount rates, bank liquidity and credit to the public and private sectors, according to the exigencies of the economic situation within the Community.

3. Accordingly it may be asked whether, among various possible ways of realizing these objectives progressively, it would not be opportune to resort to

methods that not only ensure "concertation" but at the same time permit the Community to introduce as soon as possible mechanisms, that by any test are indispensable, for attaining the final stage.

The introduction may be gradual. During the first phase the accent would be on the problem of coordinating intervention by the central banks with a view to reducing fluctuations in the rates of exchange between their currencies; during other phases new objectives could prompt coordinated action by the central banks, namely the progressive realization of Community management of the reserves and of a Community monetary policy.

On this point the introduction at a given moment of a Community organ managed by the Governors of the central banks might prove to be more efficacious in ensuring the progress to be achieved than simple "concertation" between central banks.

In fact, this organ, situated at the centre of the activity of the central banks, would have at its disposal the whole body of information; managed on a collegiate basis by the Governors it would provide a better comprehension of the Community problems; and as it developed it would enable progress to be made towards achieving smoothly the total suppression of the margins, the management in common of the reserves and the elucidation of a really "Community" monetary policy.

It is a delicate matter to decide at what moment the establishment of such an organ would be most useful. On this subject opinions may differ and the experts, considering it is a question of a political option rather than a technical question, have nothing to say in the matter.

They think, however, that on the assumption that the creation of such an organ would be accepted, it would be necessary to realize it in several successive phases depending on the experience acquired, the degree of harmonization attained in economic policy and the closeness of the cooperation developed between central banks.

2) *Creation of a Community organ*

As has been said above, the establishment of such an organ would be effected in successive phases spread over a period. These phases would not necessarily coincide with the "stages" referred to in Mr Werner's report. They might, according to circumstances, be shorter than, equal to or longer than those.

The passage from one phase to another would depend in particular on the progress achieved on the economic front and on the ease or difficulty with which the system operates, so facilitating the transition to the next phase.

First phase

In the first phase "concertation" would be effected directly between the central banks, which would every day inform an "agent" of the balance of exchange operations effected. This would enable the "agent" to centralize and sum up the total of operations effected. He would inform each central bank, which would thus have a documentary basis that would considerably assist "concertation".

The introduction of this first phase would go hand in hand with the "direct concertation between central banks" described in section B above.

Second phase

In a second phase the "agent" would suggest possible transfers between central banks in currencies of the Community and in dollars, a central bank "A" holding currency "B" exchanging it with another central bank "C" against currency "D" or dollars.

These operations would also enable a central bank to exchange a Community currency that it was holding against its own currency held by another central bank.

The operations envisaged in this second phase do not in principle entail any granting of credit. They could equally be undertaken concurrently with the "direct concertation between central banks" described in section B above, for example at the moment when it is decided to intervene jointly in dollars and in Community currencies.

Third phase

In this third phase the "agent" would favour the inter-Community mobility of the dollars accumulated within the Community: he would operate in such a way that dollars accumulated by one or more central banks would be put at the disposal of central banks short of dollars. A pool of dollars at the outset would not be essential and the system would only operate to the extent that deficits and surpluses of dollars occurred within the Community. The claims and liabilities established in this way would be guaranteed against exchange risks and could be settled at prescribed intervals either in dollars or in other reserve instruments.

That would not oblige the "agent" to open accounts in units of account at the central banks. Those that handed over dollars would show among their assets a bilateral claim guaranteed against exchange risks on the borrowing central bank.

These operations would entail the granting of bilateral credits or possibly recourse to the system of monetary support at short term, which however entails its own methods of intervention and control.[1] They would not necessarily be obligatory. There might be an advantage at any given moment in making them obligatory when cohesion within the Community has been sufficiently reinforced.

These operations would be submitted to normal processes of consultation. Their advantage would be the better to equalize the position in dollars within the Community and to avoid the accumulation of dollars by certain countries while others are losing them so showing a position of double disequilibrium in relation to the United States while the Community as a whole would be in equilibrium.

Although entailing the granting of credit, which would be on a bilateral basis, the operations envisaged in the third phase — especially if they were not obligatory — could go hand in hand with the "direct concertation between central banks" described in B above.

Fourth phase

1. In the preceding phases the role of "agent" has been limited to assembling information on the operations and suggesting transfers or compensation transactions. He only effects statistical registrations, holds no part of the reserves and exercises no action that could put pressure on the central banks.

On embarking on the fourth phase an important advance would be made.

The role of "agent" would be replaced by a "Community organ" the functions of which would be appreciably different.

The experience acquired and the progress realized in the matter of harmonization of economic policies, in the same way as that recorded in the cooperation constantly reaffirmed by the central banks, would decide the moment at which it would be possible to embark on this fourth phase.

2. The fourth phase would be characterized by the creation of a Community organ placed under the authority of the Governors. It could be instituted either by the central banks or by inter-governmental agreement, the execution of which would be entrusted to the central banks according to legal formulae to be examined later. The role of this organ would be to emphasize the Community character of the actions undertaken in the preceding phases, to establish

[1] It is well to recall three characteristics of this system:
— grant of credit on an "ad hoc" basis,
— financing founded on a quota basis,
— inauguration of a procedure of special consultation.

Community management — no longer simply a concerted one — of foreign exchange operations, to permit standardization of reserve policies leading up to a progressive pooling of reserves, and to facilitate the gradual establishment of a Community monetary policy.

The Community organ to be formed, being called on to retain and manage a part, at the outset a small one, of the reserves of the central banks, will be referred to henceforth as the "Fund".

Its first duties would be aimed essentially at a simple regularization of foreign exchange operations. With the development and progress realized towards the creation of an economic and monetary union, its functions would expand until it gradually became the organ conducting the Community management of the reserves, when it would confer on the Council of Governors, which would assume control of it, a role analogous and an authority similar to those of the Federal Reserve Board.

3. The Fund could work on the following general lines:

(i) The operations of the Fund would be expressed in units of account based on gold, defined in such a way as to indicate the individuality of the EEC.

(ii) The Fund would be furnished with an adequate reserve by transfers of dollars or other reserve elements from the central banks which, by way of counterpart, would be credited in units of account.

The central banks would not be in the position of shareholders in the Fund but would hold part of their net reserves in the form of a credit balance guaranteed by the Fund. In addition, the Fund could, in case of need, be similarly furnished with Community currencies.

(iii) The central banks would intervene in their foreign exchange markets, in dollars or in Community currencies, within the framework of the directives laid down by "concertation", all freedom of action being safeguarded as long as the rates for the dollar in the different markets in the Community remained within the Community "band".

(iv) The intervention balances in the markets, in dollars or in Community currencies, would be "transferred" each evening to the Fund against a credit of units of account in the case of a surplus, or "drawn" from the Fund against a debit of units of account in the event of a deficit. These payments or drawings of Community currencies would similarly give rise to an entry to the debit or credit of the central bank issuing them. In this way the accounts of the Fund would systematically record the movement in the reserves resulting from interventions in the market.

(v) The positions in account with the Fund would be subject to settlement at intervals to be agreed (daily, monthly or quarterly). Intervening settlements would be provided for when the debit or credit position of an account exceeded, at any given moment, a maximum sum to be determined. The credits between member countries represented by the appearance of positions on their accounts bearing different signs could be substituted for the mechanism of monetary support at short term and could be used in conjunction with financial assistance at medium term, for example, to ensure their elimination.

(vi) The Fund would be managed by a "Council of Governors of central banks". This Council would ensure "concertation" in a similar manner to that described in section B and according to the same principles, but its activities would be extended progressively from the simple establishment of the "Community level" to questions relating to the management in common of the reserves and the coordination of the monetary policies.

This development assumes in particular a previous study of conditions for harmonization of the use of the instruments of monetary policy; it also assumes a genuine will, with political backing, to arrive at a real Community management in everything that concerns the action of the central banks.

Progress in these directions should go hand in hand with that realized on the plane of harmonization of short-term and medium-term economic policies.

4. (i) This formula does not deprive the central banks of any of their prerogatives; from the moment that the "concertation" described in section B is accepted, greater cooperation between them becomes necessary. That this is effected in the form of the management of a "Fund" does not entail any new restriction on their liberty of action but offers on the contrary the advantage of getting them more used every day to being aware of the primacy of Community interests over those of a purely national nature.

(ii) The Fund would make it possible to determine automatically from day to day the variation in the official exchange reserves of each member country, and consequently to detect rapidly the appearance of any disequilibrium reflected in the external payments situation of certain countries. It would then be possible to examine to what extent the position was counterbalanced by the development of the foreign assets and liabilities of the commercial banks or was due to a disturbance of the balance of payments. This examination effected at Community level would make it possible to intervene in time with a member country so that it could adopt the measures of adjustment necessary and conform to the needs of harmonization of economic policy.

(iii) The adoption of a unit of account would confirm the autonomy of the Community. Created and defined at the time of the constitution of the Fund, the use of this unit of account could be extended to private transactions and in particular to the new issues effected in the markets of the member countries of the Community.

(iv) The dollars accumulated by the Community in excess of their current requirements would be retained by the Fund instead of being distributed among the central banks. The employment of these dollars would be negotiated at the Community level and would cease to be the subject of bilateral arrangements.

(v) The establishment of the Fund would put in their place in an embryonic form, but one susceptible of development, the instruments and mechanisms necessary for the exercise of the functions that would evolve at a later stage into an organism of the Federal Reserve Board type, in particular the Community management of foreign exchange relations with foreign countries and the management of the reserves. The Fund would make it possible to attain this last phase of the process by a progressive development of techniques and practices.

(vi) Finally, the establishment of the Fund would be a tangible manifestation of the Community's will to integrate.

(vii) The creation of the Fund and its successive developments, in particular the extent to which it decided on a progressive increase in the proportion of the reserves to be managed on a common basis, corresponding to the grant through its intermediary of reciprocal credits, would go hand in hand with the progress realized in the matter of harmonization of economic policies. Its action, however, in the immediate detection of positions of disequilibrium and the necessity that would arise from its very existence of restoring excessive credit or debit positions to a normal level, would constitute an important element making it possible to obtain more rapidly from the member countries the necessary decisions in the matter of economic policy in order to achieve closer alignment of this policy within the Community.

5. The experts consider, without however pronouncing on the political expediency of creating a "Fund" or on the date on which this could come into operation, that it would be useful to continue the examination of it on a basis at once deeper and more extensive in conjunction with other studies, notably those aimed at the harmonization of monetary policies.

Conclusions

On the conclusion of their studies the experts consider that on the technical plane it would be possible, in reply to the questions raised by Mr Werner, to envisage the following gradual process, which presupposes that sufficient progress would at the same time be made in the harmonization of economic policies:

1) A first step towards the establishment of a specific system of foreign exchange in the Community would be for the central banks acting in concert

to restrict "in fact" the fluctuations between their currencies within narrower margins than those resulting from the application of the margins in force for the dollar. The objective would be achieved by concerted action in relation to the dollar.

2) In a second phase, a reduction in the margins would be announced and concerted action would be undertaken in relation to the dollar, which would be completed eventually by intervention in Community currencies at the limit of the margins.

3) At a later stage concerted action in relation to the dollar might be supplemented by intervention in Community currencies at the limit of and within the margins.

4) The adoption of the action described in 2) and 3) above could be accompanied by recourse to an "agent", who might be the BIS, to whom would be entrusted the task of recording the balances of the operations effected in the markets of the member countries of the Community, of aggregating them and notifying them every day to each central bank, and of suggesting the possible transfers in Community currencies and in dollars, as well — if the central banks agree to grant one another bilateral credits — as the compensating operations in dollars.

5) As soon as the techniques described in 1) to 4) above are working normally and without friction, which assumes a closer harmonization of economic policies, it would seem to be technically possible to pass on to the phase characterized by the establishment of a "Fund".

The experts think that the study in depth of the conditions of creation and operation of this Fund is worth undertaking, in conjunction with other studies, notably those aimed at the harmonization of monetary policies.

Annex 1

LETTER FROM Mr WERNER TO BARON ANSIAUX CHAIRMAN OF THE COMMITTEE OF GOVERNORS OF THE CENTRAL BANKS OF THE MEMBER STATES OF THE EEC

12 June 1970

"During its meeting of 9 June, the Council of Ministers of the European Communities took cognizance of the interim report on the realization of economic and monetary union which I presented to it on that occasion. The Council took note of the conclusions in the report. It appears from the debates that the fundamental objectives described in the document met with agreement from the Governments. Nevertheless, the Council has stated that it is desirable to go more deeply into certain aspects of the suggestions made, notably as regards the steps to be taken in the course of the first stage.

On the one hand, it seems necessary to present concrete recommendations in the matter of economic and monetary policy.

On the other hand, as regards the progress to be accomplished in the monetary field, the Council of Ministers would wish to be more fully informed on certain technical and economic aspects of the proposals presented to it.

Like other colleagues who have expressed this view, I consider that on this point it would be fitting to have an opinion from the Committee of Governors of the central banks. I should therefore be grateful if you would invite the Committee over which you preside to send me its views on the following questions:

Chapters I to VII and VIII except 4th phase[1]

(i) What in the first stage would be the features of a specific foreign exchange regime peculiar to the currencies of the Member States ? In particular, what would be the advantages and disadvantages both on the economic plane and on the monetary plane of a restriction of the margins between the currencies of the member countries of the Common Market; and what would they be in the event of the dollar no longer being utilized as the intervention currency, which would reduce the possibilities of fluctuation from 3% to 1 1/2% at the maximum ?

1 References to the "Report on questions put by the *ad hoc* Committee presided over by Mr Werner."

Chapter VIII Section C 2) 4th phase	(ii) As regards the establishment of a foreign exchange stabilization fund as described in Annex 4 of the report, what would be the advantages and disadvantages in seeing progress reports on the monetary objectives of the Community ? It would be necessary to adduce arguments in favour of its creation during the first stage or make out a case for either its total elimination or its establishment at a subsequent stage.
Chapter VIII Sections B and C 2) except 4th phase	Failing the creation of such a fund during the first stage or a subsequent stage I should like to know what can and should be done here and now with a view to tightening the monetary bonds uniting the member countries of the Community and to enable it to finish up with the creation of a monetary regime based on the constitution of a "European Reserve Board" and a "European Reserve Fund" in the period laid down of ten years.
Introduction	(iii) Independently of the two preceding questions it is necessary to examine what ought to be accomplished in any case in the course of the first stage in order to tighten up effectively the monetary policies of the member countries, including in this the harmonization of the instruments of monetary policy now at their disposal.

In order to permit the Group over which I preside to draw firmly based and realistic conclusions from the mass of information furnished, I should be particularly grateful if you would ensure that the replies, even if they conflict, are as precise as possible and supported by pertinent arguments raised by one side or the other.

I am aware of the special effort that I am calling for from the members of the Committee, since these questions will demand a very high degree of concertation and concentrated study. However, you will not fail to appreciate the political necessities that oblige my Group to present its final report in the month of September. For this reason I should be obliged if you would ensure that your Committee presents its report to me by 15 July at the latest.

Thanking the members of the Committee in advance for their best endeavours in response to this letter,

I have the honour to be your obedient servant.

(signed) Pierre WERNER

Annex 2

QUESTIONS PUT BY THE AD HOC COMMITTEE PRESIDED OVER BY Mr WERNER

I. Reduction in margins for fluctuations between Community currencies

Chapter V, 1) Chapter VIII Sections A, B and C 2) 1st phase	1. In what way could a preliminary phase be introduced without a definitive undertaking being entered into immediately, for example by informal arrangements between the central banks regarding the coordination of their day-to-day interventions in the foreign exchange market ?
Chapter VI	2. In the event of an engagement to reduce the margins of fluctuation being taken: what would be the advantages and disadvantages that would result from the different possibilities presented by the intervention techniques (for example, intervention with regard to all the other currencies of the Member States; standardized intervention in relation to the dollar) ?
Chapter VII Section 1) a)	3. Would the reduction in the margins of fluctuation necessitate the granting of specific credit facilities ?
Chapter VII, Section 1) a) Chapter VII, Section 1) b)	4. What are the repercussions on the reserve requirements that would arise on the one hand from a reduction in the margin of fluctuation as such, and on the other hand from the establishment of a system of compensation and granting of credit which might possibly result from it ? Would intervention in relation to the whole of the currencies of the Member States also have repercussions on the nature and management of the reserves ?
Chapter VII Section 2)	5. What would be the consequences of a reduction in the margins of fluctuation: a) on the relations between rates of interest and the policy for interest rates in the Member States ? b) of the movement of forward rates on the policy of exchange rates in relation to other countries ?
Chapter VII Section 3)	c) on the application of the agricultural policy ?
Chapter IV	6. What would be the advantages and disadvantages of a progressive reduction in the margin of fluctuation between the currencies of the Member States as opposed to the suppression of the margins at one stroke once the convergence of economic policies between the Member States has progressed sufficiently ?

II. Exchange regularization fund

Chapter VIII Section B Chapter VIII Section C 2) 4th phase 3) and 4)	1. Is the creation of an exchange regularization fund essential in the event of a reduction in the margins of fluctuation between member countries ? Would an exchange regularization fund facilitate the current intervention that might turn out to be necessary in the national foreign exchange markets, and in what way ?
Chapter VIII Section C 2) 4th phase 4) b) and g)	2. To what extent is it considered that movements on accounts in the exchange regularization fund would serve as a warning signal of incipient disequilibrium in foreign trade more surely and rapidly than other indications of the trend of foreign trade (for example, foreign exchange positions).
Chapter VIII Section C 2) 4th phase 3) b), d) and e)	3. To what extent and in what way would it be necessary to provide the exchange regularization fund with reciprocal lines of credit furnished by the member countries ?
Chapter VIII Section C 2) 4th phase 3) e)	4. What would be the relationship between these lines of credit and the credit mechanisms at short and medium term existing or in course of preparation within the EEC ? Is it possible that, if the need arose, the necessary lines of credit needed for settlements within the exchange regularization fund would coincide with the lines of credit provided in application of the other mechanisms ?
Chapter VIII Section C 2) 4th phase 4) c) and d)	5. To what extent would the independence of the currencies of the member countries vis-à-vis the dollar be increased by the fact that the settlement of balances of exchange operations is effected through a regularization fund instead of being effected on the bilateral plane or by a technical financial agent (for example the BIS) ?
Chapter II Chapter VII 1) a)	To what extent would such independence be reinforced by a reduction or the suppression of the margins ?
Chapter VIII Section C 2) 4th phase 4) a) b) e) and g)	6. What are the possibilities for a better coordination of monetary policies by the member countries as a result of the existence of an exchange regularization fund ? In particular, what would be the advantage of such coordination in relation to arrangements permitting better consultation and a higher degree of coordination within the Committee of Governors of the central banks ?

Chapter VIII Section C 2) 4th phase 4) b) d) Chapter VIII Section C 2) 4th phase 3) d) and e) Chapter VIII Section C 2) 4th phase 3) c)	7. What would be the advantages and disadvantages of a complete or partial centralization of the currency reserves of the member countries with an exchange regularization fund; what would be the consequences of this for intervention in dollars or other third currencies effected on national markets ? In particular, could or should such intervention in relation to the dollar in national markets be effected by the regularization fund and according to what technical procedure ?
Chapter VIII Section C 2) 4th phase 3) and 4)	8. What would be the essential tasks delegated to the exchange regularization fund ? How would it be managed ?
Chapter VIII Section B	9. Failing the establishment of an exchange regularization fund, according to what techniques could cooperation in foreign exchange matters be effectively reinforced between the member countries of the Community during the first stage ?

Annex 3

COMPOSITION OF THE COMMITTEE OF EXPERTS

Chairman	Baron H. ANSIAUX
Deutsche Bundesbank	Mr E. BLUMENTHAL Mr G. JENNEMANN
Banque Nationale de Belgique	Mr J. MERTENS de WILMARS Mr F. HEYVAERT
Banque de France	Mr M. THÉRON Mr R. FLOC'H
Banca d'Italia	Mr F. MASERA Mr F. FRASCA
Nederlandsche Bank	Mr P.C. TIMMERMAN Mr A. SZASZ Mr J.A SILLEM
Commission of the European Communities	Mr F. BOYER de la GIRODAY Mr H. WORTMANN Mr A. LOUW
Secretariat of the Werner Committee	Mr G. MORELLI Mr G. LERMEN
Secretariat of the Committee of Governors	Mr A. BASCOUL Mr R. GROS

The Committee has held six sessions: 25 June, 1 and 2 July, 9 July, 16 July, 23 and 24 July, 30 July 1970.