

COUNCIL / COMMISSION
OF THE EUROPEAN COMMUNITIES

**INTERIM REPORT ON
THE ESTABLISHMENT BY STAGES OF
ECONOMIC AND MONETARY UNION**

«Werner Report»

COUNCIL — COMMISSION
of the European Communities

**The establishment by stages of economic
and monetary union in the Community**

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THE ESTABLISHMENT BY STAGES OF ECONOMIC AND MONETARY UNION IN THE COMMUNITY: INTERIM REPORT TO THE COUNCIL AND THE COMMISSION

I. INTRODUCTION

In accordance with instructions issued by the Conference of Heads of State or Government held in The Hague on 1 and 2 December 1969 and with the terms of reference contained in a decision of the Council of Ministers dated 6 March 1970, the Working Party presents its first report.^{1 2} It is an attempt to show what fundamental choices must be made if economic and monetary union is to be achieved, by stages, in the Community. The basis for the report has been an analysis of suggestions made by the Governments and the Commission's memorandum to the Council.

What follows is not a reflection of the separate and individual preferences of the members of the Working Party: the report tries to provide a joint reply despite the fact that on certain points opinions still differ. The ideas in it are put forward solely on the individual responsibility of the members of the Working Party.

No stage-by-stage plan can be worked out without a preliminary scrutiny of the present situation, so that the point of departure can be clearly defined and so that shared ideas as to the state of the economic and monetary union at the end of the stage-by-stage plan can be developed. Once the two extreme limits of the projects have been described, the report sets down the fundamental principles and certain concrete proposals on the basis of which the process which is to lead the Member States to economic and monetary union can be approached in a first stage. Subsequent studies carried out by the Working Party should provide a fuller picture of what is envisaged for the first stage and further material concerning the plan. In this way the Working Party's assignment will be completed in coming months.

II. THE POINT OF DEPARTURE

Since the signing of the Treaty of Rome, the European Economic Community has completed a number of stages of the greatest importance on the road to its economic integration. Outstanding among these are the establishment of the customs union and the definition of a common agricultural policy.

¹ The chairman of the Working Party is Pierre Werner, Prime Minister and Minister of Finance in the Government of the Grand Duchy of Luxembourg.

² See Annex 1, The Hague communiqué; Annex 2, Terms of reference of the Working Party; Annex 3, Composition of the Working Party.

However, one effect of integration is that general economic disequilibria in the member countries affect directly and quickly the overall development of the Community. Experience in recent years has shown clearly that these disequilibria are liable to undermine integration achieved in the fields of liberalization of the movement of goods, services and capital. This applies especially to the common agricultural market. There are still disparities between the member countries in respect of the achievement of growth and stability objectives, and there is still a danger that disequilibria may occur if economic policy is not effectively harmonized.

The growing interpenetration of the economies has weakened the independence of the short-term economic policies pursued in the member countries. It has become all the more difficult to implement economic policy because the loss of independence at national level has not been offset by the creation of Community policy. Here is clear evidence of shortcomings and disequilibrium in the process of building up the Common Market.

Past efforts have not been completely in vain but they have not led in fact to co-ordination or effective harmonization of the economic policies in the Community, although this is what the Treaty of Rome implies and what could have been achieved through the application of the basic clauses of the Treaty, notably the articles on economic and monetary policy.

The first two medium-term programmes failed to produce sufficiently harmonized quantitative objectives, although without these effective co-ordination is impossible. Studies of the economic situation in the Community have often led only to recommendations worded in very general terms, even when it was in the Community interest that more specific views be expressed. Broadly speaking, the consultation procedures have not produced the hoped for results, either because they have been merely formal in character or because the Member States have used escape clauses to nullify them.

Work to liberalize capital movements and to introduce the right of establishment for banks and financial institutions has not made enough progress. The reasons for this are the lack of adequate co-ordination of economic and monetary policies and special legal or other circumstances in the individual countries.

Arrangements to enable individuals to work in a Community country other than their own without restriction of any kind are not yet completely satisfactory and no real progress has been made in the harmonization of social policies.

In its external relations, particularly in international monetary relations, the Community has so far failed to assert itself adequately through the adoption of agreed positions. The reason for this has been differences of policy or of general approach, according to case.

Despite all this, producers, dealers and consumers have adapted to the new market conditions. Multinational companies have developed, and the Euro-currency and Euro-issue markets have emerged and have achieved a considerable scale of operations. Speculative movements of capital have assumed formidable proportions. These innovations, some of which are of value, are nevertheless making it more and more difficult for the Member States to control economic trends, at the very time when the growing interdependence of the industrialized economies is highlighting the problem of the individuality of the Community.

Well aware of these problems, the Commission laid before the Council on 12 February 1969 a memorandum stressing the need for progress in the co-ordination of economic policies and in the field of monetary solidarity.

The implementation of this memorandum could well lend new strength to efforts to co-ordinate and harmonize economic and monetary policy. It would, however, provide no more than the point of departure on the road to the creation of the economic and monetary union, which must be completed as soon as possible.

III. THE ULTIMATE GOAL

The Working Party has not attempted to devise an ideal system in abstract terms. Its aim has been to single out the measures which must be adopted before an economic and monetary union can be complete. The union as described here represents a stage in a dynamic process which could well take a different form under the pressure of circumstances and of policy desiderata.

The economic and monetary union will provide an area within which goods and services, persons and capital can move unhindered and free of distortions of competition, without this creating structural or regional disequilibria.

Such a union should improve on a lasting basis the prosperity of the Community and strengthen the Community's contribution to international, economic and monetary equilibrium. Given the co-operation of unions, employers' federations and the various business and social organizations, it should, through the combined effect of market forces and of policies devised and implemented by the authorities, ensure the attainment of satisfactory growth, a high level of employment, stability, the narrowing of regional and social disparities and the protection of the environment.

Within an individualized monetary area, there must be currency convertibility, irrevocable currency parities, and complete freedom of capital movement; the exchange rate bands must be eliminated. Either the various national currencies could be maintained or a single Community currency could be created: from the technical point of view, there is very little in this, but psychological

and political considerations make a strong case for the adoption of a single currency; once this was created, it would be very difficult to revert to the old system.

Economic and monetary union cannot work smoothly and without strain unless certain responsibilities are shifted from the countries to the Community authorities. Such transfers of power would be kept down to the limits necessary to ensure the effectiveness of Community action; they are mainly those concerning the group of policies involved in the maintenance of general equilibrium. In addition, economic policy instruments would have to be harmonized in the various appropriate areas.

Medium-term quantitative objectives, mutually compatible and properly related to Common Market objectives, will have to be worked out for growth, employment, prices and external equilibrium. These objectives will be brought up to date each year on the basis of moving projections.

The broad outline of *short-term economic policy* must be agreed at Community level. Here it will be necessary to know what are the factors and pre-conditions governing the control of overall demand, notably through monetary policy and the budgets. For this purpose "normative", mutually compatible economic budgets must be established each year and their implementation supervised.

The main *monetary policy* decisions — on liquidity, interest rates, intervention on the exchanges and the management of the reserves — must be centralized. The Community must dispose of a full range of the necessary instruments, though the use to which these were put would not have to be uniform in all the countries. In monetary and financial relations with non-member countries and the international economic organizations, the Community must also have a common policy and common arrangements for representation.

In guiding the general development of the economy, *budgetary policy* is of great importance. Although at the beginning of the economic and monetary union the Community budget will certainly be bigger than it is now, its influence on economic trends will remain small in comparison with that of the Member States' budgets, the harmonized administration of which is fundamental to the cohesion of the union.

The limits within which the main budget aggregates should be fixed must be decided at Community level, having due regard to the economic situation and the structural peculiarities of each country. This must be done both for the annual budget and for planning arrangements covering several years. The key factor will be the determination of the size of the deficit or surplus and the decision as to how the deficit should be financed or the surpluses allocated. So that the authorities can adjust the trend promptly and effectively, instruments that can be handled on the basis of jointly-agreed directives should be provided.

In this field centralization for its own sake must be avoided. Authority must be transferred to the Community agencies only to the extent necessary for the smooth working of the union. Budgetary structure would be varied to fit individual requirements and would operate at several levels — the Community level, the national level, etc.

If distortions of competition are to be avoided, *taxation arrangements* will have to be harmonized to some extent. This applies in particular to the value-added tax, to taxes likely to affect capital movements and certain excise duties. While enabling the fiscal frontiers to be eliminated, measures to harmonize taxation must allow of enough elasticity for taxation policy to remain effective at the various levels.

Structural disparities could well be a dangerous threat to the achievement of overall economic equilibrium. Co-operation between the Community partners in the field of *structural policy* will help to overcome these difficulties, while at the same time allowing distortions of competition to be eliminated. Financial offsetting measures will make it easier to solve the key problems in this field. Structural and regional policies cannot be implemented solely under the national budgets. Environment problems — technical, financial, social — arising out of industrial growth and urban development should be dealt with at Community level.

The cohesion of the economic and monetary union cannot be ensured if incomes in the various member countries develop on lines diverging too widely. The pattern of income trends must be carefully monitored and discussed at Community level with the *participation of both sides of industry*. More generally, unions and managements should be closely associated in the preparation and execution of Community policy. This will help to ensure the success of undertakings embarked upon jointly.

As for *institutional reform*, an economic and monetary union cannot be created without the establishment or adaptation of a number of Community agencies, to which the powers now held by the national authorities will have to be transferred. These shifts of responsibility represent a process of fundamental political importance entailing the progressive development of political co-operation in the various fields.

The Working Party prefers not to submit detailed proposals at the present time as to the form the various Community agencies should take. It is, however, important that these agencies should be able to work effectively in compliance with democratic rules, and that they should have clearly defined responsibilities and an effective power of decision.

The reform of the institutions will require amendment of the Treaty of Rome, and the preparatory work here should be carried out during the first stage. However, the Treaty, as it now stands, already allows considerable progress to be made towards economic and monetary union.

The Working Party believes that, provided the Member States maintain the political attitude towards economic and monetary union, solemnly expressed at the Hague Conference, this objective can be achieved in the seventies.

IV. IMPLEMENTING THE STAGE-BY-STAGE PLAN: PRINCIPLES

When describing above the point of arrival, the Working Party was seeking to establish clearly and accurately the final goal to be achieved. There should be no ambiguity in this respect, for economic and monetary unification is an irreversible process which should only be set in train if there is a firm determination to carry it through to its conclusion by accepting all its economic and political implications.

This definitely does not mean that economic and monetary union can be achieved overnight. On the contrary, it must be gradually built up by continuing work begun to strengthen the co-ordination of economic policies and monetary co-operation.

Between the point of departure and the final goal, measures must be adopted under a set of related headings: the establishment of overall economic guidelines, the co-ordination of short-term economic policies through money and credit arrangements, through the budget and taxation and through incomes policy, the adoption of Community policies on structure, the elimination of exchange fluctuations between the Community currencies, greater stability in parity relationships, the harmonization of external monetary policy, the integration of the capital markets, etc. All this will require in the first place fuller co-ordination of national policies, then their harmonization through the adoption of agreed directives, and lastly the transfer of responsibilities from the national to the Community authorities. As progress is gradually made, Community instruments will have to be created to take over from or underpin the national instruments.

In all the fields, the measures to be taken are interdependent and will strengthen each other; in particular, the development of monetary unification must be closely related to adequate progress in the co-ordination, and later unification, of the economic policies.

While pursuing economic and monetary unification, the Community must assert its own economic and international policy objectives vis-à-vis the outside world. While adjusting internal structure, the Community must continue to take part, through its member countries or in its own right, in those measures to liberalize trade, to further economic and monetary co-operation and to help the developing countries which are agreed at world level. Here, the economic and monetary union will have served to enhance the international

division of labour and not to form a new autarchic bloc within the international economy.

The Hague communiqué states that the plan for achieving economic and monetary union by stages should be worked out "on the basis of the memorandum presented by the Commission on 12 February 1969." The Working Party therefore took the view that the measures recommended by this memorandum formed the points of departure for the whole process, and that accordingly the Council should agree by the end of 1970 on the two points still outstanding in the memorandum, i.e. the fixing of the quantitative objectives in the third medium-term programme and the establishment of medium-term financial assistance arrangements.

Starting from these principles, the Working Party has attempted to clarify the main measures to be contemplated during the first stage with a view to strengthening the habits of working together adopted by the national authorities and to setting up the necessary machinery. These measures will constitute the corner-stone of the undertaking and a manifestation of the political determination of the Member States to commit themselves, with no going back, along the road to economic and monetary union.

During the first stage, preparatory work on adapting and amplifying the Treaty must be completed, so that subsequently commitments of growing importance can be assumed and so that Community institutions and instruments can be mobilized to control economic development in the Community. In this way transition to the full economic and monetary union will be ensured.

V. THE FIRST STAGE

The measures proposed for the first stage will, by themselves, require a major effort from the Member States and the Community. While all precipitate action must be avoided, a deadline must be set if the enterprise is to win credibility and to progress smoothly. From the technical point of view, the Working Party believes that a period of three years is the right length of time.

General arrangements

Consultation procedures will be strengthened: in more and more cases consultation will be organized before any decision to be taken and will be compulsory, and the powers conferred on the Community institutions will be used fully. Consultation will cover medium-term economic policy, short-term economic policy, budgetary policy, monetary policy and the use of other economic policy instruments: it should lead to the formation of decisions in the Member States consonant with agreed attitudes.

The Working Party will discuss at a later date ways and means of ensuring that the consultations are effective.

In the field of medium-term economic policy, quantitative objectives for each member country would have to be fixed, in respect of growth, employment, prices and the external account. Expressed as "bands" (with maximum and minimum), they would have to be brought up to date at regular intervals to serve as a point of departure for moving projections.

Work to achieve these objectives will have to be supported by the co-ordination of short-term economic policy. Within the framework of Article 103, regular scrutinies of the current economic situation in the Community, and the establishment at Community level of compatible annual economic budgets and the implementation of an early warning system will have to be arranged.

The main guidelines of economic policy, especially of income policy, will be adopted after consultation of unions and employers' associations.

Budgets

A good deal of work will have to be done on the co-ordination and harmonization of budget policy. In this connection, the greatest importance attaches to the methods chosen to finance deficits or utilize surpluses. In relation with the economic situation of each country, quantitative guidelines will be fixed for the main components of the national budgets, notably overall revenue and expenditure, for the distribution of expenditure between investment and consumption, and for the budget outturn — surplus or deficit — and its size.

To give these guidelines sufficient authority at political level, a new procedure will be established entailing preliminary discussion at Community level of the overall guidelines of the national budgets, then an examination of the main budget aggregates in the Council of Ministers, followed by a recommendation to be annexed to the draft budgets laid before the Member States' parliaments by the governments. This procedure would also be used for any important amendments to the budgets. In addition, the Council of Ministers should also monitor the implementation of the budgets.

With a view to facilitating these tasks, preliminary work on the harmonization and synchronization of national budget procedures should be undertaken without delay.

Taxation

At the present time free competition among firms is still hampered in the Common Market by disparities between tax-law requirements in the different countries. In this connection, progress must be made on the harmonization of indirect taxes, of excise duties and of those direct taxes affecting appreciably capital movements,

Internal monetary and credit policy

The interests of the Community and of its members demand that general guidelines should be worked out in common in respect of monetary and credit policy, especially with regard to liquidity, lending to the public and private sectors and interest rates. In this connection, incompatibilities between the monetary and credit policy instruments available to the member countries should be gradually ironed out.

Consultations between the monetary authorities will take place whenever a member country contemplates important domestic policy measures and whenever financial or monetary difficulties emerge in the Community. These consultations must lead to the adoption of opinions or recommendations. Measures must be taken to ensure the necessary degree of co-operation between the authorities responsible for general economic policy and the monetary authorities at Community level.

External monetary policy

During the first stage consultation procedures on external monetary policy should be strengthened: this will give practical expression to the policy of solidarity among the member countries in the determination of their currency parities.

This consideration should also apply should the International Monetary Fund authorize wider bands around the parities. If necessary, the member countries should adopt the specific measures needed to maintain the fluctuations of intra-Community rates within their present confines. A more fully concerted monetary policy should also cover the granting and utilization of credit, including, for example, drawings on the International Monetary Fund and swap credits, the creation of new liquidity in the form of increased quotas or further development of the special drawing rights, and the foreign currency holdings of the banks. The first step should be taken towards the gradual establishment of EEC delegations to the IMF and the other international financial agencies.

Despite general agreement upon the points outlined above, certain options are still open.

(i) Certain members of the Working Party feel that whatever else is done the Community should also, in the first stage, be given an independent exchange system of a kind that would serve to assert the Community's personality in its dealings with the rest of the world. This system could be based on an *initial reduction in the permitted bands* between the member countries' currencies — the range of fluctuation is at present double that of the range of each of these currencies against the dollar. If the reduction is small it will not appreciably affect the flexibility of monetary policy instruments, while reducing the prefer-

