

would also be necessary over the use of subsidies, and the Union would have to have the right to require the discontinuance and scaling down of any internal tax which discriminated against imports from other countries in the Union and of any consumption tax which bore severely on Union imports of which there was no home production. There would have to be also a close Union interest in State trading to ensure that the I.T.O. rules, designed to secure non-discrimination as between the members and to limit protection of home industry, were strictly observed.

5. It would not be easy to bring about the necessary measure of joint action. It is doubtful whether democratic Governments would be willing to give such powers to an international body. If so, there is a strong presumption that if a Customs Union were to survive it would have to move towards a full Economic Union with a single economic and financial policy.

6. Entry into any close Economic Union with the countries of Western Europe, and the consequent removal of restrictions of all kinds on trade between the members of the Union, would require substantial adjustments in many policies which we regard as fundamental, in particular, the system of imperial preference and the sterling area arrangements as well as our policy for home agriculture.

Imperial Preference

7. From the outset we have given great attention to the possible effect of a European Customs Union on the market for goods from other Commonwealth countries. It will be remembered that in the course of the discussions of the Havana Charter the United Kingdom Delegation succeeded in securing a revised draft of the Article dealing with Customs Unions. This revised version has already been incorporated in the General Agreement on Tariffs and Trade. It provides that preferences "shall not be affected" by the formation of a Customs Union but "may be eliminated or adjusted by means of negotiations between affected countries (including countries outside the Union). Further, the Article now permits the International Trade Organisation (or, in the case of the General Agreement on Tariffs and Trade, the contracting parties) by a two-thirds majority to approve proposals for a Customs Union not fully complying with the rules otherwise applicable. All this gives considerable flexibility and leaves to future negotiations the treatment within a Union of preference systems as a whole or of individual preferences. In any such negotiations involving the United Kingdom the other Commonwealth countries could take part. It would be essential to have these negotiations before a commitment was taken by the United Kingdom to enter a Customs Union, and a settlement of the preference problem on lines satisfactory to all countries concerned is a *sine qua non* of our even considering entering a Customs Union. We have made this clear to the countries participating in the Brussels discussions.

8. It is impossible to forecast with confidence how the eventual arrangements would work out. It might prove possible to secure some small departure in our favour from the strict rules. In some cases we might be able to maintain a diminished preference for Commonwealth countries by retaining some duty against Union members. In others we might have it accepted that long-term contracts should afford a certain preference to Commonwealth goods. In some cases the common tariff might be so arranged as to give higher preferences in the United Kingdom over all but Union members. But there is a danger that the other members of the Union could not or would not be willing adequately to compensate the other Commonwealth countries for their loss of preferences in the United Kingdom.

9. The studies referred to in paragraph 2, as to the effects which a Customs Union might have on certain sectors of production, had to be based on certain assumptions about preferences. The assumptions were that where a member of the Union now gives preferences, it is deemed to continue to give such preferences as against other countries which are not members of the Union but not as against the members; except that where goods now enter a country on preferential terms free of duty, they can be deemed to continue to do so. Where before the formation of a Union a member has been giving preferences, any preference which it is deemed to continue to give after the formation of a Union is not deemed also to be given by the other members of the Union. Quota preferences are deemed to have been abolished. These assumptions were, however, only working hypotheses