

DUBLIN EUROPEAN COUNCIL

13 and 14 DECEMBER 1996

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I.

INTRODUCTION

The European Council, meeting in Dublin on 13 and 14 December 1996, took a number of significant decisions for the continued development of the European Union.

The European Council:

- achieved further decisive progress on Economic and Monetary Union,
- identified a broad range of measures to be implemented at national and Community level aimed at boosting employment,
- adopted the Dublin Declaration on Employment,
- welcomed the general outline for a draft revision of the Treaties submitted by the Irish Presidency as a good basis for the final phase of the Intergovernmental Conference which should conclude at Amsterdam in June 1997,
- adopted an important series of measures in the area of Justice and Home Affairs and, in particular, agreed ways and means to combat the scourges of drugs, organized crime, including terrorism, and the sexual exploitation of children,
- reviewed the Union's action in external relations.

The European Council began its proceedings by an exchange of views with Mr. Klaus HÄNSCH, President of the European Parliament, on the main subjects for discussion at this meeting. It thanked Mr. HÄNSCH, who will be stepping down from office next January, for his valuable contribution to furthering constructive cooperation between the Institutions.

A meeting also took place today with the Heads of State or Government and the Ministers for Foreign Affairs of the associated countries of Central and Eastern Europe, including the Baltic States, as well as Cyprus. There was a broad exchange of views on these conclusions and on matters pertaining to the field of Justice and Home Affairs, with particular reference to the fight against drugs and organized crime.

II. ECONOMIC AND MONETARY UNION

1. Economic and Monetary Union

The European Council welcomes the further decisive progress which has been made in the preparations for EMU, which will begin on 1 January 1999.

- The structure of the new Exchange Rate Mechanism has been agreed.
- The urgent aspects of the legal framework for the use of the euro have been finalized for early adoption.
- The principles and main elements of the Stability and Growth Pact for ensuring budgetary discipline in EMU have been agreed.

The European Council therefore urges the institutions, public authorities and economic agents to intensify their preparations for the starting date of 1 January 1999.

The European Council welcomes the excellent Report by the ECOFIN Council (annexed) on preparations for Stage 3 of EMU, which is fully in line with the conclusions of Madrid and Florence, and it pays tribute to the contributions, in their respective fields of competence, from the Commission and the European Monetary Institute (EMI). The contents of this Report are subject to Parliamentary reservations.

In particular the European Council:

- endorses the conclusions on **the new exchange rate mechanism** (ERM2) as proposed by the ECOFIN Council and the EMI. It invites the ECOFIN Council to prepare for the European Council in June 1997 a draft Resolution setting out the fundamental elements of the ERM2, following the precedent set in 1978 in relation to the present ERM. The EMI is invited to prepare, in parallel, a draft for an inter- central bank agreement, for

submission to the European Central Bank and the central banks of the Member States not forming part of the euro area.

- underlines the need to ensure durable budget discipline in Stage 3 of EMU and welcomes the agreement reached on the **Stability and Growth Pact**. It requests the ECOFIN Council to examine intensively the Commission proposals for two Regulations, one on the strengthening of the surveillance and co-ordination of budgetary positions and the other on speeding up and clarifying the implementation of the excessive deficit procedure. It invites the Commission to put forward a proposal for a Regulation on non-participating Member States. Furthermore, it invites the ECOFIN Council to prepare a draft Resolution on the Stability and Growth Pact to be adopted by the European Council in June 1997, recording the commitments of the Member States, the Commission and the Council to a strict application of the Treaty and the legal provisions on budgetary stability. The European Council notes that after it has adopted the Resolution, the Council will adopt the respective Regulations.
- welcomes the agreement by the ECOFIN Council on the two Regulations establishing the **legal framework for the euro** which are being made public by the Presidency. It invites the Council to adopt the first Regulation based on Article 235 of the EC Treaty without delay. The second Regulation will be adopted by the Council as early as possible in 1998, once the decision on the Member States participating in the euro area has been taken.

The Council, meeting in the composition of Heads of State or Government, has taken its decision under Article 109j(3) of the EC Treaty and confirms that the procedure laid down in Article 109j(4) will be applied as early as possible in 1998, with a view to the commencement of the third stage of EMU on 1 January 1999. In this context, the European Council welcomes the intentions of the Member States to further reduce budgetary imbalances in 1997 with a view to achieving the high degree of sustainable convergence required for participation in the single currency and it underlines the need for durable convergence in the third stage.

The European Council underlines the importance of exchange rate stability for the process of convergence and the smooth operation of the internal market and accordingly warmly welcomes the entry into the ERM of the Finnish markka on 12 October 1996 and the re-entry of the Italian lira on 24 November 1996.

The European Council underscores the need to make the euro tangible for citizens. In this regard, it welcomes the designs for the euro bank notes presented by the European Monetary Institute. It also welcomes the arrangements being made by the Commission for the design competition for the coins; this will allow the choice to be made during the Dutch Presidency.

The Heads of State or Government decided to reappoint Baron Alexandre LAMFALUSSY as President of the European Monetary Institute as of 1 January 1997 until 30 June 1997. They decided to appoint Dr. Willem Frederik DUISENBERG, President of De Nederlandsche Bank, as President of the European Monetary Institute as of 1 July 1997 until the establishment of the European Central Bank.

2. SEM 2000 (Sound and efficient management)

The European Council endorsed the Council conclusions of 2 December 1996 on the report of the Personal Representatives Group on Sound Financial Management.

It reaffirmed its support for the Commission's SEM 2000 initiative and generally welcomed the recommendations in the report which constitute a substantial action programme to improve the financial management of EU expenditure in partnership between the Commission and the Member States.

The European Council invited Council and Commission to report on progress in implementing the recommendations to its meeting in December 1997.

III. EMPLOYMENT

1. Growth and Employment in Europe - the way forward

The fight against unemployment is the prime responsibility of the Member States but also a priority task of the Union. The European Council had an in-depth discussion on the growth and employment strategy, based on the joint report from the Council and the Commission on employment, the Commission's progress report on the initiative for "Action on employment: a Confidence Pact" and the joint contribution by the social partners on the Confidence Pact which they adopted in Dublin on 29 November. In its deliberations it has also taken account of the proposals in President Chirac's Memorandum on a European Social Model with a view to giving greater emphasis to the human dimension of the Union.

The European Council, building on the Essen strategy, endorses the analysis contained in the Joint Report and urges the Member States to pursue this strategy with determination and consistency. It calls for continued support for this strategy by all relevant actors at European, national and local level, including the social partners and reaffirms the importance of equal opportunities.

To underline its commitment to this strategy the European Council has adopted the **Dublin Declaration on Employment** (annexed), which reflects the recommendations in the Joint Report on the need for:

- a continuation of the macroeconomic strategy for economic growth and employment in line with agreed economic policy guidelines,
- increased efforts to modernize the markets for goods and services and to exploit new sources of employment,
- a focusing on labour market efficiency and on investment in human resources,

- making taxation and social protection systems more employment-friendly,
- strengthening the interplay between macroeconomic and structural policies in the Member States' Multiannual Employment Programmes.

It invites the Commission and the Member States, especially in the framework of the new Employment and Labour Market Committee and the Economic Policy Committee, to develop further the instruments for the effective monitoring and evaluation of employment and labour market policies and the identification of good practice. In particular, common employment indicators should be further developed and the possibilities of benchmarking should be assessed.

The European Council welcomes the positive reaction to the initiatives on territorial employment pacts and urges swift implementation of the 60 projects proposed by the Member States.

The European Council stresses once again the essential role of the Internal Market in promoting growth and employment in the Union. Enhancing the competitiveness of small and medium-sized enterprises has a crucial role to play to this effect. Whilst noting the progress that has been accomplished in this area, it remains concerned with the delays in the transposition and implementation of a number of Directives. It takes note of Commission's intention to submit before the Amsterdam European Council an action plan and a timetable covering all necessary measures that must be taken to ensure that the full potential benefit of the Internal Market is achieved before the beginning of Stage 3 of EMU.

The European Council noted the Commission report on the development of tax systems, which was drawn to its attention by the ECOFIN Council, underlining the need for further work on this issue. The European Council welcomed the Commission's intention to continue the discussions in a tax policy group, paying particular attention to the effects of this policy on employment.

The European Council welcomes the Commission's plans in relation to innovation and the development of the information society as important inputs for the future development of the Union's competitiveness. Investment in education and training are crucial for securing equal opportunities for all citizens to participate in and benefit from the information society. The European Council believes that there should be regular monitoring and evaluation of the Union's competitiveness against world best practice along the lines of the conclusions on benchmarking adopted by the Industry Council.

The European Council reiterates the importance of regulatory simplification and requests, in this context, the extension of the Simpler Legislation for the Internal Market (SLIM) initiative. It emphasizes that the effort to reduce administrative costs for enterprises, particularly small and medium-sized enterprises, is necessary for Member States as well as the Community institutions and invites the Council to follow up in this respect its resolution on legislative and administrative simplification in the internal market.

Postal services form an essential component of the communications infrastructure in the Union. The development of the internal market for postal services bears huge significance in economic and social terms. The European Council welcomes the intensive efforts made to date to effect relevant measures, but notes with regret that the Council has not reached a Common Position. It

asks the Council to take a decision by the end of the year, taking account of the work already done at its meeting on 28 November 1996.

The European Council asks the European Parliament, the Council and the Commission to take all steps so that an immediate decision to liberalize postal services can be taken. The universal service in the postal sector must remain assured.

The European Council recognizes the importance of the implementation of the Trans-European Networks. It agrees with the proposal by the Portuguese and Spanish Governments that priority project No. 8 in list 1 from the Essen European Council will become the Multimodal link between Portugal/Spain and the rest of Europe.

2. Subsidiarity and Proportionality

The European Council reaffirms the importance of ensuring that the institutions apply subsidiarity and proportionality thoroughly to all legislative proposals. It welcomes the Commission's 1996 "Better Law Making" report on the application of subsidiarity and proportionality, on simplification and on consolidation of legislation. The European Council invites the Commission to provide a progress report before the end of 1997.

IV. THE INTERGOVERNMENTAL CONFERENCE

The European Council welcomed the general outline for a draft revision of the Treaties submitted by the Presidency. This makes it possible for the negotiations to move now into their final phase.

The European Council has also taken note of the recent letter from the German Chancellor and the French President which will be an important contribution to the further work of the Conference.

The European Council reaffirms the importance of completing the Conference at Amsterdam in June 1997. The Presidency document provides a good basis for the work which lies ahead. As the document makes clear, delegations remain free to advocate their own proposals and to press their concerns in further negotiation.

As it moves now into its final decisive phase, the Conference must seek to achieve a balanced outcome in all areas which will measure up to the aims and ambitions which the European

Council has set for it. It is essential that the Union be equipped to face the challenges ahead as it prepares for the 21st century.

The European Council notes with approval the progress at the Conference in identifying Treaty changes which would make the Union more responsive to the concerns of its citizens and it reaffirms the aims which it set out at Florence in this regard.

The European Council notes with approval the particular importance which the Presidency document attaches to the area of Justice and Home Affairs. The European Council has agreed today on a number of important decisions under the existing Treaty provisions which are set out in Section V of the present conclusions. It asks the Intergovernmental Conference, taking account of the outline draft for Treaty revision presented by the Presidency, to work to reach agreement on a strengthened capacity for action in relation to visas, asylum, immigration, the crossing of external borders, the fight against drugs and international crime including terrorism, offences against children and trafficking in persons. Europol should have operative powers working in conjunction with the national authorities to this end. These issues are of the most serious concern to citizens in all Member States and the Union must be given the means to act effectively in these areas.

The European Council also reaffirmed the aim which it set in Florence of developing the external action of the Union. The Union must enhance its capacity to ensure that its external action is coherent and effective in all its aspects, and it must improve its decision-making procedures, if it is to play a role in the world commensurate with its responsibilities and its potential. The European Council noted the approaches which the Presidency has identified in its document in relevant areas including the options for establishing a new function to enhance the visibility of the CFSP and the strengthening of links with the WEU.

Institutional issues will be central to the next phase of the negotiations. The Union needs to improve its ability to take decisions and to act. This is already true today and it will be even more necessary as the Union moves to enlarge its membership further. The Union must have comprehensible, transparent and democratic procedures and strong and effective institutions which enjoy legitimacy in the eyes of its citizens.

The European Council notes that the Presidency document, responding to a view of many delegations that certain issues can be settled definitively only at a later stage in the Conference, does not include texts in Treaty form on the issue of flexibility and on certain sensitive institutional questions, although it offers an analysis of the issues and identifies options. In the next phase of the Conference solutions must be found on all institutional issues, including in particular on the size of the Commission, the role of the European Parliament, the collective association of national parliaments, the voting mechanisms in the Council and the functioning of the Court of Justice, while respecting the balances which have always been an important feature of European construction.

The European Council also notes the progress made thus far in examining the proposals for Treaty provisions which would permit more flexible approaches leading to enhanced cooperation

in appropriate areas, subject to agreed conditions. This issue is of great importance and the European Council asks the Conference to devote particular attention to it.

The European Council emphasizes strongly that the future of the Union and the success of the further enlargement to which it has committed itself will depend on a satisfactory resolution of all of these questions.

The European Council asks the Conference to develop the important proposal to amend the Treaties to establish it as a clear principle that no citizen of a Member State of the Union may apply for asylum in another Member State, taking into account international treaties.

The European Council notes also the proposal submitted jointly by three delegations, since the presentation of the Presidency document, for the Treaty to include the specific character of the outermost regions of the Union and it asks that it be examined by the Conference.

Finally, the European Council asks the Conference, on the basis of the preparatory work already carried out, to continue to work to present a significantly simplified version of the Treaties with a view to making them more readable and comprehensible to the Union's citizens. This must be done in a way which does not reopen the *acquis* of the Treaties, preserves the pillar structure and does not delay the outcome of the Conference.

V. JUSTICE AND HOME AFFAIRS

The European Council reaffirms its commitment to maintain and develop the European Union as an area of freedom, security and justice by putting to full use all of the instruments provided for in the Treaty on European Union.

1. Fight against drugs

The European Council welcomes the report from the Council on the substantial progress made since its last meeting in Florence and endorses the proposals for action contained in this report.

The European Council welcomes, as a concrete expression of a shared political will, the agreement which has been reached on a Joint Action on the approximation of the laws and practices of police, customs services and judicial authorities in the fight against drug addiction and illegal drug trafficking, and the resolutions on sentencing for serious drug trafficking offences, on combatting drug tourism and on drug production and cultivation. It also welcomes the adoption of the Programme for Community action on the prevention of drug dependence.

The European Council stresses that this constitutes a first step and that the momentum achieved must be maintained and further developed on those bases, in particular through:

- continued examination of further harmonisation of laws, insofar as an agreed need for it is identified, complemented by reinforced cooperation between the Institutions and the Member States. In this context, the particular dangers posed by synthetic drugs deserve special attention;
- continued review of further cooperation between law enforcement agencies to combat drug trafficking;
- full application of the Directive on money laundering and its possible extension to those relevant professions and bodies outside the classical financial sector;
- development by the Council and the Commission of the contribution which research activities can make in addressing the medical, socio-economic and detection aspects of drug abuse;
- energetic implementation of the action plan to combat drugs in the Caribbean, as well as the implementation of the agreed follow-up of the report by the expert mission to Latin America;
- further development of the structured dialogue with the associated countries of Central and Eastern Europe in regard to drugs issues; comparable cooperation with the Russian Federation, initiated during the current Presidency, should be pursued;
- following a proposal by President Chirac and Prime Minister Major, to examine ways to assist Central Asian republics, utilizing the TACIS programme, to fight transit in and production of drugs.

Cooperation with transatlantic partners in these fields has also to be continued and, where appropriate, improved.

The European Council confirms the priority it attaches to sustained and coordinated action in the fight against drugs making full and coherent use of all the instruments of the Union.

It invites the Council to draw up by the end of 1997 a first assessment of measures undertaken, with a view to strengthening and supplementing them.

2. Fight against organized crime

The European Council underlines its absolute determination to fight organized crime and, to this end, stresses the need for a coherent and coordinated approach by the Union.

The European Council welcomes the report made by the Presidency on stepping up the fight against organized crime and decides to create a high level group to draw up a comprehensive Action Plan containing specific recommendations, including realistic timetables for carrying out the work. The Group should examine the fight against organized crime in all its aspects on the clear understanding that it would refer any issues involving Treaty change to the Intergovernmental Conference which is addressing Treaty changes in this area as a priority. The high level group should complete its work by March/April 1997.

In order to implement rapidly the measures proposed in the report made by the Presidency, the European Council asks the Council to reinforce its Secretariat, by setting up a team of specialized national experts and practitioners, seconded for a limited duration.

As a practical step in combating international crime, the European Council urges the ratification at the earliest possible date of the Customs Information System, Fraud and Extradition Conventions and their Protocols, as well as, by the end of 1997, of the Europol Convention and its subsequent Protocol. It also highlights the importance of bringing to a rapid conclusion the convention on Mutual Assistance in Criminal Matters.

The European Council urges the Council and the Commission to take effective and coherent action to address the abuse of new communications technologies, including the Internet.

3. Sexual exploitation of children and trafficking in human beings

The European Council expresses its abhorrence at the sexual exploitation of children and trafficking in human beings and undertakes to take all necessary action to protect those most vulnerable in society. It welcomes the agreement on a joint action defining a common approach to offences against children and improving judicial cooperation. Other joint actions aimed at enhancing police cooperation by widening the competencies of the Europol Drugs Unit and creating centres of expertise in investigating such crimes were adopted. Community funds have been made available for fighting these odious crimes.

The European Council calls on the Council and the Commission to implement actively these instruments and to consider necessary further action.

4. Fight against terrorism

The European Council condemns unreservedly all terrorist attacks and continues to pay close attention to the threat posed by terrorism both internally and externally. For this reason the EU is working closely with other international partners and international organizations to review and update measures already adopted against this threat and adopt, where necessary, new measures. For this reason the Member States reiterate their will to cooperate closely on the matter; the European Council emphasizes the need to do so.

5. Racism and Xenophobia

The European Council welcomes the progress made since its meeting in Florence and calls on the Council to complete its work with a view to the speedy establishment of a European Monitoring Centre on Racism and Xenophobia which will have to work in close cooperation with the Council of Europe.

6. External frontiers

The European Council draws again attention to the need to resolve speedily the remaining questions regarding the draft Convention on crossing by persons of the External Frontiers of Member States of the European Union.

VI. ENLARGEMENT

The Commission informed the European Council on its progress on the opinions and other reports related to enlargement as requested of it at Madrid. The European Council welcomes the assurance given by the Commission that these documents as well as the communication on the future financial framework of the Union will be available immediately after the conclusion of the Intergovernmental Conference. It confirms the timetable for the enlargement process as set at its Madrid meeting. The European Council takes note of the Council's report on the implementation of the pre-accession strategy in the second half of this year. It also notes the Commission's endeavours to strengthen the present implementation of this strategy. Moreover it welcomes the Commission's intention to present proposals for an overall reinforcement of the pre-accession strategy together with its opinions and other reports under preparation.

VII. EXTERNAL ACTION BY THE UNION

The European Council adopted the declarations on [Former Yugoslavia](#) and the [Middle East Peace Process](#) at annex.

RUSSIA

The European Union expresses its solidarity with the Russian people as they implement their historic choice in favour of democracy, the rule of law and a market economy. The European Council reiterates the Union's readiness to assist the Russian Federation in meeting the difficult challenges ahead, notably through the Partnership and Cooperation Agreement, the EU/Russia Action Plan and by bringing Russia as soon as possible into the WTO and other international fora.

The European Council warmly welcomes President Yeltsin's important decision to withdraw all Russian troops from Chechnya and the recent agreement between Chechen leaders and the Russian Prime Minister. It notes the intention to hold elections in Chechnya on 27 January 1997. The European Council expresses its continuing support for the important work of the OSCE Assistance Group in Chechnya.

UKRAINE

The European Council welcomes the adoption by the Council of the Action Plan for Ukraine which demonstrates the importance which the Union attaches to its relations with Ukraine and its desire to develop closer cooperation in the framework of the Partnership and Cooperation Agreement.

The European Council recalls its firm attachment to the implementation of the memorandum of understanding reached with Ukraine on the definitive closure of the Chernobyl nuclear power station by the year 2000. It welcomes the closure by the Ukrainian authorities of reactor number one as an important step in this direction.

BELARUS

The European Union is seriously concerned at developments in Belarus, in particular relating to the referendum on the new Constitution. The European Union wishes to see a Belarus committed to democratic principles, human rights and a market economy playing a full part in Europe. The European Council calls on the leadership of Belarus to re-establish full respect for internationally accepted democratic and constitutional principles and practices and hopes that the leadership will accept the Union's proposal for a fact-finding mission. The absence of progress in these areas would have a negative impact on relations between Belarus and the European Union and on Union support for Belarus's accession to the Council of Europe.

COUNCIL OF EUROPE

The European Council believes that the Council of Europe has a crucial role in upholding human rights standards and supporting pluralist democracy.

It sees advantage in using to the fullest, in cooperation with other international institutions, the expertise and mechanisms of the Council of Europe to advance these objectives. The summit meeting of the Organization, in 1997, will provide a significant opportunity to review the progress made in these areas.

REGIONAL COOPERATION IN EUROPE

The European Council notes the wider range of regional activities in Europe reaching from the Arctic to the Black Sea. In this context, the European Council welcomes the Commission's report on the Central European Initiative presented in response to its request at Florence. It notes that the Commission will submit regular reports to the Council on these regional initiatives.

MEDITERRANEAN

The European Council reaffirms the high priority it attaches to the European Union's Mediterranean dimension and expresses satisfaction at the significant and balanced developments in the Euro-Mediterranean partnership during the year since the adoption of the Barcelona Declaration.

In the political and security partnership, work on the implementation of the principles of the Barcelona Declaration will continue, notably through the action plan, towards the adoption of a Union-Mediterranean charter.

TURKEY

The European Council reaffirms the importance it attaches to the further development of the EU's relations with Turkey in both the economic and political fields. It notes with regret, however, that certain serious issues remain to be resolved in the relationship. The European Council welcomes the Turkish Government's stated intention to take measures to improve the human rights situation. In the context of closer partnership with the European Union it emphasizes the need for the observance of the highest standards of human rights.

The European Council invites the Presidency to continue its efforts following the Council's declaration of 15 July 1996 to promote an acceptable solution to the situation in the Aegean area in accordance with established international norms and to pursue contacts with the Turkish Government with a view to an early Association Council.

The European Council urges Turkey to use its influence to contribute to a solution in Cyprus in accordance with UN Security Council resolutions.

EU-US RELATIONS

The European Council notes that the EU-US Summit in Washington on 16 December will be the first anniversary of the adoption at Madrid of the New Transatlantic Agenda and the Joint EU-US Action Plan and expects it to be another milestone in EU-US relations. It welcomes the qualitative improvement which this represents in principle as well as in practice over the past year.

The European Council reaffirms the objectives which it shares with the US in promoting human rights, democratic values and fundamental freedoms in parts of the world where these are inadequately observed, but also its conviction that such objectives should be pursued by means other than unilateral action at the expense of close partners with shared values.

The European Council reaffirms the essential contribution which close EU-US partnership can make to international stability, security and prosperity and the importance in this context of the Transatlantic Dialogue in deepening and widening the EU-US relationship through solid cooperation between them.

EU-CANADA RELATIONS

The European Council welcomes agreement on the text of a Joint Declaration and an Action Plan, which will further enhance cooperation between EU and Canada in pursuit of common objectives and on the basis of deeply-held shared values.

GREAT LAKES

The European Council expresses grave concern about the continuing violence in the Great Lakes Region, not only in Eastern Zaire but also in Burundi. It welcomes the return of large numbers of refugees, but underlines the need to facilitate the voluntary repatriation of the remaining refugees, and to initiate rehabilitation and reconstruction efforts. It recalls the considerable efforts undertaken by the EU to meet humanitarian needs. In the meantime, the continuing

humanitarian emergency, particularly in Eastern Zaire, requires fast and decisive action by the international community. Underlining the need for a flexible approach in the light of the rapidly changing circumstances on the ground, the European Council agrees that the implications of these changes for the implementation of UN Security Council Resolutions concerning the establishment, for humanitarian purposes, of a temporary multinational force will need to be addressed rapidly. In this regard, the European Council restates the willingness of the European Union to contribute fully and urgently to these efforts, pursuant to the Joint Action of 22 November 1996, the associated Council Decision of the same date and the WEU Ministerial Declaration of 19 November 1996. It welcomes the Commission proposal for a strategic and comprehensive plan of action for EU assistance to the Great Lakes Region.

The European Council welcomes the initiative of the regional leaders in seeking to resolve the problems in Eastern Zaire through dialogue. It hopes that, at the second Nairobi Summit of Heads of State of the Region on 16 December, they can build upon the principles already agreed by them, including the crucial importance of respect for the territorial integrity and sovereignty of Zaire, in pursuit of a peaceful resolution of the conflict. Recognizing the importance of the electoral process in terms of the stability of the region, it reiterates the commitment of the Union to play its part in support of the successful completion of that process in Zaire by means of the Joint Action adopted on 11 November 1996 and looks forward to the latter's early and urgent implementation.

The European Council reiterates its view that the problems of the region as a whole can only be resolved by political means. The European Union will, in particular through its Special Envoy, continue to support the efforts of the regional leaders and to encourage dialogue between the different parties to conflict in the region. The European Council reaffirms its support for the early convening of an international conference under the joint auspices of the UN and the Organization of African Unity in order to address within a global approach the root causes of the crisis and thus bring about a peaceful, durable and comprehensive resolution of the conflicts in the region.

EAST TIMOR

The European Council welcomes the initiatives within the European Union aimed at improving the situation, living conditions and human rights of the East Timorese people. It reaffirms its support for all efforts which can contribute to a fair, comprehensive and internationally acceptable solution, which fully respects the interests and legitimate aspirations of the Timorese people in accordance with international law. It hopes that the talks under the auspices of the UN Secretary General will lead to substantial progress towards the resolution of the question of East Timor.

CUBA

The EU wishes to see progress towards a peaceful transition to pluralist democracy, respect for human rights and fundamental freedoms in Cuba, as well as economic policies calculated to bring about a sustainable recovery and an improvement in the living standards of the Cuban people. The Common Position adopted by the Council on 2 December will be pursued through a

result-oriented constructive dialogue. The EU will lend its support to progress towards democracy, including the possible negotiation of a cooperation agreement. Any agreement would, in accordance with EU practice, contain a suspension clause in the event of a serious breach of the human rights provisions.

TRANSITION IN HONG KONG AND MACAO

The European Council reiterated the European Union's strong interest in the future peace and prosperity of the Hong Kong Special Administrative Region (SAR) of the People's Republic of China to be created next July, and the European Union's desire to do anything possible to contribute to a smooth transition. The European Union is committed to strong continuing relations with the SAR in the World Trade Organization and in all other matters where the SAR will enjoy autonomy under the Basic Law. The European Council underlined the European Union's full support for the specific status of the SAR and its citizens in all respects, including their right to representative democratic institutions as already established. The European Council requested the Commission to propose in due course during 1997 how best to ensure close economic cooperation.

The European Council takes note of the positive way in which the transition process has been developing in Macao. It hopes that the implementation of the Sino-Portuguese Joint Declaration signed in 1987 will continue to contribute to the progress and social stability of the territory with a view to a smooth transfer of government in December 1999. It also hopes for the continuation of the respect for the fundamental principles of the Joint Declaration beyond that date.

WTO

The European Council noted with satisfaction the outcome of the first regular bi-annual WTO Ministerial Conference which took place in Singapore on 9-13 December 1996 and at which the European Union demonstrated once again the importance it attaches to the multilateral trading system and the efficient operation of the WTO.

The European Council expresses its satisfaction at the renewed impetus which the WTO Ministerial Conference in Singapore has given to the liberalisation of world trade. It particularly welcomes the broadening of the WTO work programme to encompass issues which the European Union had identified as priorities. It also welcomes the breakthrough on trade in information technology products and urges the fullest possible participation by third country partners in the final agreement to be reached by 15 March 1997. The European Council also welcomes the continued momentum towards a successful conclusion of the negotiations on basic telecommunications in February 1997.

The European Council welcomes the launch by the Commission of a new market access strategy and calls for enhanced and coordinated efforts by the Community and Member States to open up third country markets.

With regard to the report on the evolution of the trade policies and preferential agreements of the Community, the European Council took note that the Council would finalize it in its February session with a view to presenting it at Amsterdam.

VIII. SEATS OF OFFICES AND AGENCIES

The European Council noted the progress which has been made in the implementation of its decision taken in Brussels in October 1993 on the location of Agencies and Offices. The Council endorsed the Commission's decision of 10 December 1996 to arrange for the early transfer of the staff of the OICVP to Ireland initially and specifically thereafter to Grange, Co. Meath in premises to be made available at that location by the Irish authorities.

The European Council urged that appropriate measures be taken by the different institutions to ensure that the required resources are made available to implement the Commission's decision.

The Council also notes the conclusions of the Agriculture Council of 18 November 1996 as regards staffing of the OICVP and urged that appropriate measures be taken by the different institutions to ensure that the required staffing resources are made available to enable the Union to discharge its supervisory responsibilities.

Addendum

The European Council has noted the following reports from the Presidency/Council:

- Council report on achievements in the field of Justice and Home Affairs
- Presidency report on stepping up the fight against organized crime
- SEM 2000 (sound financial management): Council Conclusions and report of the personal Representatives Group

The European Council also noted the following reports from the European Commission:

1. Europe as an Economic Entity
2. The impact and effectiveness of the single market
3. Putting services to work
4. Europe at the forefront of the global information society
5. The first action plan for innovation in Europe
6. Europe's place in the world: fourth report of the Ciampi group

7. Trans-European Networks
8. Better Lawmaking (report on the application of the subsidiarity and proportionality principles, on simplification and on consolidation).

DUBLIN EUROPEAN COUNCIL

13 and 14 DECEMBER 1996

PRESIDENCY CONCLUSIONS: ANNEXES

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ANNEX I

ECOFIN COUNCIL

Dublin, 13 December 1996

REPORT ⁽¹⁾ BY THE ECOFIN COUNCIL TO THE EUROPEAN COUNCIL THE PREPARATIONS FOR STAGE 3 OF EMU

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Introduction

1. The European Council in Madrid a year ago confirmed that 1 January 1999 will be the starting date for Stage 3 of Economic and Monetary Union (EMU) in accordance with the convergence criteria, timetable, protocols and procedures laid out in the Treaty ⁽²⁾. Accordingly, the European Council requested the Council:

- to study, together with, in their respective fields of competence, the Commission and the European Monetary Institute (EMI), the range of issues raised by the fact that some countries may not initially participate in the euro area; in particular, the study should cover those issues related to monetary instability;
- to work on ways to ensure that, after moving to Stage 3, public finances are kept on a sound track in line with Treaty obligations. The European Council stated that budgetary discipline is of crucial significance both for the success of Economic and Monetary Union and for the acceptance of the single currency by the public; it noted the Commission's intention to present in 1996 its conclusions on ways to ensure budgetary discipline.

It requested the Council to report on these issues as soon as possible.

Furthermore, the Madrid European Council requested the Council to complete, at the latest by the end of 1996, the technical preparation of a Council Regulation on the legal framework for the use of the euro.

2. The Council has worked accordingly on all three issues and expects to be ready to decide on them at the same time. It has received substantial assistance from the Commission and the EMI in their respective fields of competence. The Council submitted a progress report to the European Council in Florence which urged the Council to pursue its work with a view to presenting conclusions showing further substantive progress to the European Council in Dublin. The informal meeting of Ministers and Governors in Dublin in September made further progress on these issues. On 16 October, the Commission adopted proposals for legislation on the legal framework for the euro and on budgetary discipline in Stage 3. The European Monetary Institute has prepared a report on monetary and exchange rate relationships in Stage 3 which the Council commends and attaches to this report.

3. An exchange rate mechanism would provide Member States having a derogation with a reference for their conduct of sound economic policies in general and monetary policy in particular. The Council therefore presents **proposals for a new exchange rate mechanism (ERM 2)** in Stage 3 of EMU. The details are described in **Chapter I** of this report and in the EMI report.

4. The Council sees a strong link between the exchange-rate issues and budgetary discipline and therefore considered both issues in parallel. Monetary policy cannot, without adequate support

from fiscal and other policies, achieve its objective of price stability and secure that lasting convergence which fosters stable exchange rates. It needs adequate and sustained support from fiscal and other policies. A Stability and Growth Pact to ensure strict budgetary discipline on an enduring basis is therefore essential.

The Council, in its progress report to the European Council in Florence, has already submitted the outline of such a pact. Since that meeting, the Council has continued to work on this issue, and is now in a position to submit its suggestions for the **main elements of a Stability and Growth Pact**, including a possible European Council Resolution, in accordance with the procedures and principles of the Treaty. They are contained in **Chapter II** of this report.

5. In its work on the **legal framework of the euro**, the Council has been particularly reliant on assistance from the EMI and the Commission. The technical preparation for legislation was significantly advanced at the informal meeting of the Council in September. **Chapter III** reports on the state of preparation for legislation.

I. Relationships between Member States in the euro area and those outside in Stage 3

6. In its work on the relationship between the Member States forming part of and those not forming part of the euro area, the Council was guided by principles laid out in its progress report which was adopted by the Florence European Council. There it was agreed :

- that all Member States, whether adopting the euro or not, have a strong common interest in the good functioning of economic and monetary union and of the exchange rate mechanism. As a consequence, all Member States will be involved in the dialogue on the issues raised by the move to Stage 3 of EMU, including monetary and exchange-rate matters as well as institutional and budgetary issues;
- that a stable economic environment is necessary for the good functioning of the single market and for higher investment, growth and employment and is therefore in the interest of all Member States.

7. Over recent months, the Council has continued to work on these aspects of relationships between Member States forming part and those not forming part of the euro area. In so doing, it has sought to build on and to strengthen the unity which the Community has achieved and in particular to ensure that the relevant Community bodies continue to work effectively and harmoniously.

8. In the Council's progress report to the European Council in Florence, it was stated that the proper functioning of the single market must not be endangered by real exchange-rate misalignments, or by excessive nominal exchange-rate fluctuations, between the euro and the other EU currencies, which would disrupt trade flows between Member States. Lasting

convergence of economic fundamentals is a prerequisite for sustainable exchange-rate stability. To this end, there is agreement that in Stage 3 of EMU all Member States must pursue disciplined and responsible monetary policies directed towards price stability. The co-ordination of monetary policies in the framework of the ECB General Council will therefore play a central role. Sound fiscal and structural policies in all Member States are, at least, equally essential for sustainable exchange-rate stability.

9. The report adopted in Florence also made it clear that an exchange-rate mechanism can help to ensure that Member States orient their policies to stability foster convergence among the Member States not participating in the single currency, and thereby help them in their efforts to adopt the single currency. At the same time, it could also protect them and participating Member States from unwarranted pressures in the foreign-exchange markets. In such cases, it may assist non-participating Member States, when their currencies come under pressure, to combine appropriate policy responses, including interest rate measures, with co-ordinated intervention. And it would help to ensure that Member States seeking to adopt the euro after 1 January 1999 receive a treatment equal to that of those initially participating with respect to the fulfilment of the convergence criteria.

10. In view of these considerations, the European Council accepted that it is indeed appropriate that a new exchange-rate mechanism should replace the present ERM as from 1 January 1999. It would reflect lessons and experience gained with the present system and provide continuity. Sufficient flexibility would need to be allowed, in particular to accommodate the varying degrees, paces and strategies of economic convergence of the non-euro area Member States joining the mechanism ("the other participants"). Membership would continue to be voluntary. Nevertheless, Member States with a derogation can be expected to join the mechanism.

The new exchange-rate mechanism (ERM 2)

11. ERM 2 will be based on central rates, defined vis-a-vis the euro which will be at the centre of the system. The standard fluctuation band will be relatively wide, like the present one. Through the implementation of stability-oriented economic and monetary policies, the central rates will remain the focus for the participating Member States. Central rates and the standard fluctuation band will be set by mutual agreement between the Ministers of the euro-area Member States, the ECB and the Ministers and Governors of the central banks of the non-euro area Member States participating in the new mechanism, following a common procedure involving the European Commission, and after consultation of the Economic and Financial Committee. The Ministers and Governors of the central banks of the Member States not participating in the exchange-rate mechanism would not have the right to vote in the procedure.

12. Intervention at the margins will in principle be automatic and unlimited, with very short-term financing available. However, the ECB and the central banks of the other participants could suspend intervention if this were to conflict with the primary objective of maintaining price stability. It should be ensured that any adjustment of central rates is conducted in a timely

fashion so as to avoid significant misalignments. All parties to the agreement, including the ECB, would have the right to initiate a confidential procedure aimed at reconsidering central rates.

13. The exchange-rate policy cooperation between the ECB and the central banks of the other participants could be further strengthened, for example by allowing closer exchange-rate links between the euro and the other currencies in ERM 2, where, and to the extent that, these are appropriate in the light of progress towards convergence. The procedure to be followed would depend on the form of the closer link. The initiative to agreeing to such links would lie with the non- euro area Member State concerned. The existence of such closer links, in particular if it implied narrower fluctuation bands, would be without prejudice to the interpretation of the exchange-rate criterion pursuant to Treaty Article (EC) 109j.

14. ERM 2, just as ERM 1, will require co-ordination of economic and monetary policies. The Treaty provides a good basis for the dialogue on assuring stability.

- As regards Member States' economic policies, Treaty Article (EC) 103 defines the framework for co-ordination at Community level. It provides for the discussion and adoption by the Council of broad guidelines of economic policies, and it sets out arrangements for multilateral surveillance of economic developments and policies in order to ensure closer co- ordination of economic policies and sustained convergence of economic performance. Moreover, if and as long as there are Member States outside the euro area, the Economic and Financial Committee will have the task of assisting the ministers in their monitoring of the operation of ERM 2 as well as keeping under review the monetary and financial situation of these Member States and reporting regularly thereon to the Council and the Commission.
- At the level of the central banks, the ECB General Council will monitor the functioning of the exchange-rate mechanism and will serve as a forum for monetary and exchange-rate policy co-ordination as well as for the administration of the intervention and financing mechanism.

While close co-operation between the Community bodies in the conduct of these various exercises will be necessary and useful, the division of responsibilities will need to respect the independence of the ECB and the non-euro area NCBs.

15. The main operational features of the new exchange-rate mechanism are described in the EMI paper annexed to this report.

A framework for stability

16. All Member States have mutual interests and obligations in the monetary field. Indeed, the Treaty states that each Member State shall treat its exchange-rate policy as a matter of common interest. As was reconfirmed in the Council's report to the European Council in Florence cited

above, lasting convergence of economic fundamentals is a prerequisite for sustainable exchange-rate stability.

17. For all Member States, the surveillance procedures as described in paragraph 14 will seek to ensure that their domestic policies are geared to price stability and sound public finances, thus creating the conditions for keeping exchange rates stable. While membership of ERM 2 remains voluntary, Member States with a derogation can be expected to join the mechanism and thus to have a central rate vis a vis the euro, thereby providing a reference point which assists in judging the adequacy of their policies. Member States outside ERM 2 and thus not having a central rate will present policies, so as to enable appropriate surveillance in the Council, which can make, when necessary, non binding recommendations under Article 103, and in the General Council of the ECB. This surveillance will seek to ensure that their policies are oriented to stability and thus to avoid real exchange rate misalignments and excessive nominal exchange rate fluctuations. In this way, the provision of Treaty Article (EC) 109m, whereby each Member State shall treat its exchange rate policy as a matter of common interest, can be given effect. The policies will be presented in the convergence programmes.

The Council and the Commission are considering further the methods for the effective surveillance of exchange rate developments.

II. Ensuring budgetary discipline in Stage 3 of EMU (Stability and Growth Pact)

18. The Treaty imposes on Member States in Stage 3 of EMU an obligation to avoid excessive deficits ⁽³⁾. Sound government finances are crucial to preserving stable economic conditions in the Member States and in the Community. They lessen the burden on monetary policy and contribute to low and stable inflationary expectations such that interest rates can be expected to be low. They are an essential condition for sustainable and non-inflationary growth and a high level of employment.

19. To that end, the Council proposes to adopt regulations on the strengthening of surveillance and budgetary discipline and on speeding up and clarifying the excessive-deficit procedure. These regulations, combined with a European Council Resolution, will constitute a Stability and Growth Pact. The Resolution would enshrine the solemn political commitment of the Commission, the Council and the Member States to the strict and timely application of the pact. The surveillance procedure and the excessive-deficit procedure (except, in particular, sanctions) will be common to all Member States. Euro area Member States will be obliged to submit stability programmes and will be subject to agreed sanctions for failure to act effectively on excessive deficits. In the surveillance procedure, the other Member States will be obliged to submit convergence programmes only. In the excessive-deficit procedure, sanctions cannot be applied to them.

20. In this chapter of the report, the Council submits the main elements of the Stability and Growth Pact. A credible and effective pact will ensure budgetary discipline in Stage 3 of EMU in accordance with the principles and procedures of the Treaty, while in no way changing the requirements for the adoption of the euro, either in the first group or at a later date.

Reinforced surveillance of budgetary positions

21. Each Member State will commit itself to aim for a medium-term budgetary position of **close to balance or in surplus**. This will allow the automatic stabilizers to work, where appropriate, over the whole business cycle without breaching the 3 per cent reference value for the deficit. This was agreed by the European Council in Florence.

22. Member States adopting the euro will be required by secondary legislation to present **stability programmes**, which will specify their medium-term budgetary objectives, together with an adjustment path for the government surplus or deficit ratio and the expected path for the government debt ratio. Furthermore, the programmes will contain the main assumptions about economic developments as well as a sensitivity analysis of the deficit and debt position and explain what is being done to achieve the objective.

23. A separate legislative proposal will be forthcoming from the Commission which will provide for the submission of **convergence programmes** by the non-euro area Member States. The information they will contain, as far as budgetary policy is concerned, will be similar to that of the stability programmes.

24. Member States will commit themselves to take the action they think necessary to achieve the objectives of their programmes. Stability and convergence programmes will be multiannual and will be updated annually to take account of the latest available information. Member States will make their stability and convergence programmes public.

Early warning system : monitoring and surveillance

25. The Commission and the Council will study these stability and convergence programmes and monitor Member States' budgetary performances with reference to their medium-term objectives and adjustment paths with a view to giving **early warning** of any significant deterioration which might lead to an excessive deficit. In such cases, the Council will address recommendations to the Member State concerned.

Excessive deficit procedure

26. Adherence to the objective of sound budgetary positions close to balance or in surplus will allow a Member State to deal with normal cyclical fluctuations while keeping its government deficit within the 3 percent reference value. Nevertheless, to deter excessive deficits and to ensure that, should they occur, they are promptly eliminated, there is a need for detailed provisions for the implementation of the excessive-deficit procedure. A Council Regulation will provide for expediting and clarifying the procedure, in particular by establishing clear definitions and setting deadlines for the various steps. Once it has decided that an excessive deficit persists, and as long as a Member State has failed to comply with a decision under Treaty Article (EC) 104c(9), the Council will, in accordance with paragraph 11 of that Article, impose sanctions on a prescribed scale. The European Council Resolution described in paragraph 37 will provide political guidance on how this procedure can be operated efficiently and speedily.

27. An excess of a government deficit over the 3 per cent reference value shall be considered exceptional when resulting from an unusual event outside the control of the relevant Member State and which has a major impact on the financial position of general government, or when resulting from a severe economic downturn.

28. The Commission will be invited to commit itself in the European Council Resolution (see paragraph 37) to prepare a report whenever the actual or planned government deficit exceeds the 3 per cent reference value, thereby triggering the procedure under Article 104c(3). The Commission, when preparing such a report, will consider, as a rule, an excess over the reference value resulting from an economic downturn to be exceptional only if there is an annual fall of real GDP of at least 2%.

29. The Economic and Financial Committee will formulate an opinion on the Commission report within two weeks. The Commission, taking fully into account this opinion and if it considers that an excessive deficit exists, will address an opinion and a recommendation to the Council for a decision. In the event that the Commission considers that a deficit is not excessive, the Commission will be invited to commit itself in the European Council Resolution to present in writing to the Council the reasons for its position. This would give the Council the opportunity to discuss the issue taking account of both the Commission's position and the opinion of the Economic and Financial Committee. The Council could decide, by simple majority, to request the Commission under Article 109d to make a recommendation. The Commission will be invited to commit itself in the European Council Resolution to issue, as a rule, such a recommendation, in response to the Council request.

30. The Council when deciding, according to Article 104c (6) on a Commission recommendation, whether an excessive deficit exists, will in its overall assessment take into account any observations made by the Member State showing that an annual fall of real GDP of less than 2% is nevertheless exceptional in the light of further supporting evidence, in particular on the abruptness of the downturn or on the accumulated loss of output relative to past trends.

31. Where it decides that an excessive deficit exists, the Council will, at the same time, make recommendations to the Member State concerned " *with a view to bringing that situation to an*

end within a given period" (Article 104c (7)). These recommendations will accordingly set clear deadlines for i) the taking of effective action (within four months), and ii) the correction of the excessive deficit, which should be completed in the year following its identification unless special circumstances are given. The Council's initial judgement on whether effective action has been taken will be based on publicly-announced decisions of the Government.

32. If a Member State fails to act in compliance with the successive decisions of the Council under paragraphs 7 to 9 of Article 104c, the Council will, in accordance with paragraph 11 of that Article, impose sanctions including a non-interest bearing deposit. These sanctions would be imposed within ten months of the reporting of the figures notifying the existence of an excessive deficit. An expedited procedure will be used in the case of a deliberately planned deficit which the Council decides is excessive.

33. The excessive deficit procedure will be held in abeyance if a Member State does in fact adopt, through formal government decision, appropriate action in response to a recommendation under Article 104c (7) or a notice issued under Article 104c (9). The Commission and Council will monitor the progress of the Member State continuously until the Council decides under Article 104c (12) that the excessive deficit has been corrected. If the action is not being implemented, or is proving to be inadequate, the procedure will resume immediately. This would lead to sanctions being imposed in accordance with Article 104c (11) within three months of the procedure's resumption.

34. If actual data demonstrate that an excessive deficit has not been corrected within the time limit specified either in the Recommendation under Article 104c (7) or the notice issued under Article 104c (9), the Council will immediately resume the excessive deficit procedure.

Structure and scale of sanctions

35. Whenever sanctions are first imposed, a non-interest-bearing deposit should be included. This should be converted into a fine after two years if the deficit of the government concerned continues to be excessive. When the excessive deficit results from non-compliance with the government deficit reference value, the amount of the deposit or fine will be made up of a fixed component equal to 0.2% of GDP, and a variable component equal to one tenth of the excess of the deficit over the reference value of 3% of GDP. There will be an upper limit of 0.5% of GDP for the annual amount of deposits. The amount of the sanction will be based on outcomes for the year in which the excessive deficit occurred.

36. Further consideration is being given to the disposition of the interest on deposits and the proceeds of fines on the proviso that there would be no increase in Community spending.

European Council Resolution on the Stability and Growth Pact

37. When using the leeway which secondary legislation necessarily must leave to them, the Council and the Commission may receive guidance from the European Council, through, for example, a European Council Resolution. Such a Resolution would give strong political guidance to the Commission, the Council and the Member States on the implementation of the procedures. The Resolution would invite all parties to implement the Treaty and the Stability and Growth Pact regulations strictly. The Commission should express a clear commitment to that effect, which would include an undertaking to prepare a report on the budgetary situation in a country whenever there is the risk of an excessive deficit or the planned or actual government deficit exceeds the reference value.

The Council would be invited to take the decisions necessary for carrying the procedure forward as quickly as practicable. If the Council did not act on a Commission recommendation at any stage in the procedure, the Resolution would invite the Council always to state in writing the reasons which justify its decision not to act and to make public the votes cast by each Member State. The Resolution would also cover political agreements on the implementation of the Stability and Growth Pact. In particular, the Resolution would invite the Council always to decide to impose sanctions if a participating Member State fails to take the necessary steps to bring the excessive deficit situation to an end as recommended by the Council.

The Resolution will contain an undertaking by the Member States not to invoke the benefit of the provision in paragraph 30 unless they are in severe recession. In evaluating whether the economic downturn is severe, the Member States will as a rule take as a reference-point an annual fall in real GDP of at least 0.75%.

The recitals of the Council Regulation would make an explicit reference to the Resolution.

III. Legislation establishing the legal framework for the use of the euro

38. The legal framework for the use of the euro is of the greatest importance, encompassing as it does the *lex monetae* of the monetary union and the legal provisions by which the single currency replaces the participating national currencies and the European Currency Unit (ECU).

It was agreed at the informal meeting in Dublin that it was imperative in the interests of the smooth functioning of the financial markets that certain matters be clarified on a firm legal basis as soon as possible.

39. It was accordingly decided to separate the provisions which must be enacted soon and to envisage their early adoption in a Council Regulation under Treaty Article (EC) 235. This Regulation will cover, principally, the replacement of the ECU by the euro at a rate of one to one

at the start of the third stage, the continuity of contracts when the euro is introduced and technical rules for the conversion rates, including rounding. All other provisions will be included in a Council Regulation to be adopted under Treaty Article (EC) 109I⁽⁴⁾. Although this Regulation cannot be adopted by the Council until early 1998, earlier stages in the legislative process are being completed.

This Regulation will provide, in particular, that the currency of the participating Member States shall be the euro from the first day of the third stage and that during a transitional period the euro shall be divided into national currency units; it will also regulate the introduction of euro notes and coins. Following the principle of "no prohibition, no compulsion", this legislation will at the same time regulate the use of the euro and the national currency units during the transitional period and will ensure that the monetary law of participating Member States will continue to apply, subject to the provisions of the Regulation, during that period, while national notes and coins will continue to be the sole legal tender.

40. On 16 October 1996, the Commission adopted proposals for these two Regulations. Since then these proposals have been examined intensively in a Council Working Group. There is now a text for the Regulation under Article 235 as agreed within the Council Working Group. The Group also agreed the text of the other Regulation. The provisions in articles 10 and 11 of the Regulation based on Treaty Article 109 I (4), on the circulation of euro notes and coins, provide for a date to be decided, in accordance with the Madrid scenario when the regulation is adopted : for technical reasons, it is not possible to decide this date now. Further work also remains to be done on Article 8(4).

The Council, having taken into account the opinions of the European Parliament and the EMI, endorsed the text of both Regulations on 12 December 1996.

IV. Conclusion

41. The European Council is invited to approve this report. Subject to that approval, the Council proposes the following actions :

a. The new exchange rate mechanism

The Council will present a draft Resolution for adoption by the European Council in June of next year, setting out the fundamental elements of ERM2. In this Resolution, the European Council would be following the precedent set in 1978 in relation to the present mechanism. In parallel, the EMI would prepare a draft for an inter-central bank agreement, for submission to the European Central Bank (ECB) and the central banks of the Member States not forming part of the euro area when the ECB comes into existence.

b. The Stability and Growth Pact

After the Dublin European Council meeting, the Council will establish a working group which will examine intensively the Commission proposals with a view to adoption of these Regulations immediately after the European Council, in June of next year, has adopted a Resolution on the Stability and Growth Pact, a draft of which will be presented by the Council.

c. The legal framework for the use of the euro

The urgent Regulation under Article 235 will be adopted by the Council at an early date. Formal adoption of the Regulation based on Article 109 L (4) is not possible until 1998. Together, the two regulations establish the legal framework for the use of the euro.

Annex 1 to ANNEX I

Decisions to be taken under Treaty Article (EC) 109j (3) by the Council meeting in the composition of Heads of State or Government

As part of the preparations for Stage 3 of EMU and according to Article 109j (2), the Council has to assess at the end of 1996 *for each Member State whether it fulfils the necessary conditions for the adoption of a single currency, and whether a majority of the Member States fulfil the necessary conditions*, and to recommend its findings to the Council, meeting in the composition of the Heads of State or Government. It was already clear to the European Council in Madrid a year ago, and confirmed in Florence, that at the end of 1996 there would be no majority of Member States fulfilling the conditions for the adoption of a single currency and that, therefore, 1 January 1999 (the latest date envisaged in the Treaty) would be the start date of Stage 3 of EMU.

As the basis for its Recommendation, the Council has received reports in accordance with paragraph 1 of Article 109j from the Commission and the EMI. These reports examine, as the Treaty requests, *the compatibility of each Member State's national legislation, including the statutes of its national central bank, with Articles 107 and 108 of the Treaty and the Statute of the European System of Central Banks (ESCB). The reports also examine the achievement of a high degree of sustainable convergence by reference to the fulfilment by each Member State of four criteria*. These criteria relate to price stability, the sustainability of the government financial position, the observance of the normal fluctuation margins provided for by the exchange-rate mechanism of the European Monetary System and long-term interest-rate levels.

The Council takes this opportunity to stress that the four criteria of sustainable convergence and the requirement of central bank independence must be strictly applied. This is essential if the coming completion of monetary union is to have the essential quality of stability and the euro is to be assured of its status as a strong currency. It is equally important that, when the criteria are

applied in early 1998, they are applied with a view to ensuring that government financial positions in particular are sustainable and not affected by measures of temporary effect.

The reports under Article 109j (1) indicate that many steps have been taken towards ensuring the independence of the national central banks but that in some Member States the process is not yet complete. Similarly, with regard to convergence, progress has been achieved but much remains to be done. In particular, government financial positions remain unsatisfactory in many countries : some improvements have been achieved in recent years but substantial efforts still have to be undertaken to reduce government deficits and debt.

The (Ecofin) Council has therefore made an assessment under paragraph 2 of that Article, on a recommendation from the Commission, that at present there is not a majority of the Member States fulfilling the necessary conditions for the adoption of a single currency and presents to the Council meeting in the composition of the Heads of State or Government a Recommendation for a decision to that effect and a decision that the Community will therefore not enter the third stage of EMU in 1997 and that thus the procedure laid down in Article 109j (4) will be applied as early as possible in 1998.

The Council, meeting in the composition of the Heads of State or Government will also wish to take into account the Opinion of the European Parliament.

Annex 2 to ANNEX I

EUROPEAN MONETARY INSTITUTE Report to the European Council session in Dublin on 13—14 December 1996

MONETARY AND EXCHANGE RATE POLICY COOPERATION BETWEEN THE EURO AREA AND OTHER EU COUNTRIES

Final : 7 October 1996

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INTRODUCTION

In accordance with the mandate given by the European Council meeting in Madrid and building on the agreement reached at the European Council session in Florence ⁽⁴⁾ as well as on the broad support expressed at the Informal ECOFIN Council session in Dublin ⁽⁵⁾, the EMI has finalized the first stage of its preparatory work on the future monetary and exchange rate relationships between the euro area and other EU countries. The report reflects the high level of consensus reached in the EMI Council on the objectives, principles and main operational features of the new exchange rate mechanism.

I. OBJECTIVES, PRINCIPLES AND OVERALL STRUCTURE

1. The need for monetary and exchange rate policy cooperation

Close policy coordination between the euro area and the other Member States from the very start of Stage Three of EMU is a matter of common interest and forms an integral part of the completion of the EMU process. In order to ensure the efficient functioning and development of the Single Market, it is especially important that real exchange rate misalignments between the euro and the other EU currencies be avoided, as well as excessive nominal exchange rate fluctuations, which would disrupt trade flows between Member States; hence the obligation under Article 109m to treat exchange rate policy as a matter of common interest.

The lasting convergence of economic fundamentals, in particular price stability, is a prerequisite for sustainable exchange rate stability. To this end, in Stage Three of EMU, all Member States will need to pursue disciplined and responsible monetary policies directed towards price stability. The coordination of monetary policies within the framework of the ECB General Council will, therefore, play a central role. Sound fiscal and structural policies in all Member States are, at least, equally essential for sustainable exchange rate stability. In the absence of a convergence of fundamentals, any attempt to coordinate exchange rate policies is bound to be unsuccessful. Exchange rate policy cooperation cannot be a substitute for stability-oriented domestic policies.

The final objective of economic, monetary and exchange rate policy cooperation is convergence towards macroeconomic stability, which would lead to exchange rate stability against the euro. A nominal exchange rate mechanism may provide a reference for the conduct of sound economic policies in Member States on their way towards full economic convergence. It may help to enhance the credibility of such policies by establishing a focal point for agents' expectations. Moreover, it may provide a framework for counteracting market pressures unwarranted in the light of underlying fundamentals. In particular, it may assist any Member State, the currency of which comes under pressure, to combine appropriate policy responses, including interest rate measures in the country the currency of which is under pressure, with coordinated intervention.

Monetary and exchange rate policy cooperation should be flexible enough to accommodate different degrees and strategies of economic convergence. As noted in the Conclusions of the European Council meeting in Florence, "Membership would continue to be voluntary;

nevertheless, Member States with a derogation can be expected to join the mechanism", once they have achieved a satisfactory degree of economic convergence. In addition, the various Community mechanisms for the coordination of economic and monetary policies (see also Chapter II, Section 2) should ensure that exchange rate developments in all other Member States, irrespective of their participation in the exchange rate mechanism, are closely monitored and assessed with a view to the requirements of Article 109m of the Treaty and the smooth operation of the Single Market. While the remainder of this report focuses on the exchange rate mechanism, the necessary broader scope of the overall policy coordination framework should be borne in mind.

2. Principles for an exchange rate mechanism in Stage Three

In designing an exchange rate mechanism for Stage Three, the new economic and institutional environment which is expected to prevail by that time will have to be taken carefully into account. In particular, five elements must be underlined.

First, the statutory requirement for the ECB to maintain price stability would need to be safeguarded. It would be detrimental to the credibility of EMU if obstacles were to emerge as a consequence of exchange rate oriented measures which would hinder the newly-created ECB in the pursuit of its primary objective. These considerations would also apply to the non-euro area ⁽⁶⁾ NCBs, which should also pursue the primary objective of price stability. Second, the euro is expected to play the anchor role in monetary and exchange rate policy cooperation in the EU. This will be the natural consequence, first and foremost, of the stability of the euro and the fact that member countries with a derogation are expected to put in place the conditions to enable them to participate in the euro area at a later stage.

Third, sufficient flexibility would need to be allowed, in particular to accommodate the varying degrees, paces and strategies of economic convergence of the non-euro area Member States.

Fourth, it should be ensured that any adjustment of central rates is conducted in a timely fashion so as to avoid significant misalignments.

Finally, as a matter of principle, continuity and equal treatment among all Member States with respect to the fulfilment of the convergence criteria, including the exchange rate criterion, need to be ensured.

3. Overall structure of the mechanism

Given the respective competences and responsibilities, it would be appropriate to retain the two-pillar structure of the present ERM, which is based on two parallel agreements among governments, on the one hand, and among central banks, on the other: while a European Council Resolution would form the foundation of the new mechanism, the operating procedures would be laid down in an agreement between the ECB and the non-euro area NCBs.

II. MAIN OPERATIONAL FEATURES OF AN EXCHANGE RATE MECHANISM

In the light of the abovementioned principles, the new mechanism could be designed along the following lines.

1. Central rates and fluctuation bands

The new exchange rate mechanism would be based on central rates, defined vis-à-vis the euro for the non-euro area currencies. A standard fluctuation band would be established for these currencies around their central rates. Although the exact size of the standard fluctuation band has yet to be decided, it is expected to be relatively wide.

If appropriate, non-euro area Member States could establish, on a bilateral basis, fluctuation bands between their currencies and intervention arrangements, with the aim of limiting excessive bilateral exchange rate oscillations. Prior to concluding such arrangements, the non-euro area Member States concerned would consult, on a strictly confidential basis, all the other parties to the new exchange rate mechanism.

Central rates and the standard wide band would be set by mutual agreement between the ECB, the Ministers of the euro area Member States, and the Ministers and Governors of the central banks of the non-euro area Member States, following a common procedure involving the European Commission and after consultation of the Economic and Financial Committee. The Ministers and Governors of the central banks of the other Member States not participating in the exchange rate mechanism will not have the right to vote in the procedure.

The sustainability of exchange rate relations will need to be closely monitored on a permanent basis. All parties to the agreement, including the ECB, would have the right to initiate a confidential procedure aimed at reconsidering central rates.

2. Monitoring the functioning of the system

Intra-EU monetary and exchange rate policy coordination between the euro area and the non-euro area Member States will, pursuant to the Treaty, be conceived as a continuation of the present mechanism. The Economic and Financial Committee will, together with the European Commission, be involved in economic policy coordination. Furthermore, if and as long as there are Member States with a derogation, the Economic and Financial Committee will keep under review the monetary and financial situation of these Member States ⁽⁷⁾. At the level of the central banks, the ECB General Council will monitor the functioning of the exchange rate mechanism and will serve as a forum for monetary and exchange rate policy coordination as well as for the administration of the intervention and financing mechanism ⁽⁸⁾. While close cooperation between the Community bodies in the conduct of these various exercises will be necessary and useful, the division of responsibilities will need to respect the independence of the ECB and the non-euro area NCBs.

3. Intervention and financing facilities

Foreign exchange intervention and — after appropriate use of foreign reserve holdings — financing at the standard wide margins will, in principle, be automatic and unlimited. Intervention should be used as a supportive instrument in conjunction with other policy measures, including appropriate fiscal and monetary policies conducive to economic convergence.

The ECB and the non-euro area NCBs would have the possibility of suspending intervention and financing if these were to impinge on their primary objective. In deciding whether or not to resort to this safeguard clause, the ECB or a non-euro area NCB would take due account of all relevant factors, in particular the need to maintain price stability and the credible functioning of the new exchange rate mechanism. Without prejudice to its independent assessment, in line with Articles 105 and 107 of the Treaty, as to whether there is a risk to its primary objective, the ECB would base its decision on factual evidence and, in this context, also give consideration to any conclusion which may have been reached by other competent bodies. It would appear neither advisable nor possible to define formally and ex ante the circumstances under which the possibility of suspending intervention might be used. The final decision would rest with the ECB or the non-euro area NCB concerned, but it would be understood that, time permitting, the ECB or the NCB concerned would signal as far ahead of time as possible its intention of suspending intervention and financing.

The possibility of coordinated intramarginal intervention decided by mutual agreement between the ECB, as the central bank issuing the intervention currency, and the respective NCB, in parallel with other appropriate policy responses by the latter, would be retained. As in the present ERM, unilateral intramarginal intervention would continue to be subject to prior approval by the central bank issuing the intervention currency concerned, should it exceed certain thresholds.

The present Very Short-Term Financing facility (VSTF) would be continued, following some appropriate adjustments. The initial duration (2 1/2 to 3 1/2 months), as well as the rules for extending maturities of VSTF financing operations (renewable twice for three months subject to certain ceilings and/or the agreement of the creditor central bank) would be retained. Outstanding balances would, as in the present ERM, be remunerated at a representative market interest rate corresponding to the duration and currency denomination of the credit. Financing balances would be denominated in the creditor's currency. VSTF balances would be settled in the creditor's currency, unless otherwise agreed between the creditor and debtor central banks.

The present ERM rules governing access to the VSTF facility for intramarginal intervention would be broadly continued, including the understanding that appropriate use of foreign reserve holdings would be made prior to resorting to the VSTF facility. The size of the ceilings for such access could, initially, be retained and adjusted in the light of experience of the practical operation of the mechanism.

The Short-Term Monetary Support Mechanism (STMS) should be discontinued, given its very limited practical relevance in the past. To the extent that the STMS quotas are relevant for the definition of VSTF ceilings, the latter may have to be redefined.

4. Closer exchange rate cooperation

The exchange rate policy cooperation between non-euro area NCBs and the ECB could be further strengthened. This might take various forms: inter alia, closer links may entail narrower fluctuation bands, which would be made public, with automatic intervention and financing at the narrow limits; alternatively, they may rely on informal narrower target ranges, which might be kept confidential, supported through an enhanced role for coordinated intramarginal intervention. However, a proliferation of ad hoc links should be avoided. To this effect, a standard arrangement could be used as a reference for closer links with NCBs of non-euro area Member States which have achieved a sufficiently high degree of convergence. The existence of such closer cooperation, in particular if it implied narrower fluctuation bands, would be without prejudice to the interpretation of the exchange rate criterion pursuant to Article 109j of the Treaty.

Closer exchange rate links would be agreed upon on a case-by-case basis at the initiative of the interested non-euro area Member State. The procedure to be followed would depend on the form of the closer link. Arrangements implying publicly announced narrower fluctuation bands would be agreed upon by the ECB, the Ministers of the euro area Member States and the Minister and

Governor of the central bank of the non-euro area Member State concerned, after consultation of the Ministers of the other non-euro area Member States and the ECB General Council. All other closer arrangements of a more informal nature would be agreed upon by the ECB and the central bank of the non-euro area Member State concerned, after consultation of the Ministers of all Member States and the ECB General Council.

Closer exchange rate links would be subject to progress in economic convergence, although they should not be seen as the only possible strategy to be followed by non-euro area Member States on their way towards full economic convergence. They would require a continuous monitoring of the sustainability of the closer exchange rate link and an active use of accompanying policy measures by the non-euro area Member State. All parties having agreed upon a closer exchange rate arrangement, including the ECB, would have the right to trigger a confidential re-examination of the adequacy of such a closer exchange rate link and, if applicable, to suspend intervention and financing in the event of conflict with the primary objective of price stability.

CONCLUDING REMARKS

The basic features of a mechanism to succeed the present ERM should be announced well ahead of the decision on the first wave of participants in the euro area. Thus, markets would be reassured about the continuity of monetary and exchange rate policy cooperation in the EU, preserving the role of the present ERM for non-euro area currencies during the interim period. This could help to allay any incipient market fears about the management of the exchange rates of non-euro area currencies after the start of Stage Three. Full specification of the operational details would have to await the establishment of the ECB.

ANNEX II

The Jobs Challenge

Dublin Declaration on Employment

Employment continues to be the first priority for the European Union and the Member States and their greatest challenge. The need for firm and sustained action has never been greater. While in the Union as a whole there has been a slight increase in employment over the past year, the European Council remains deeply concerned at the slow pace of progress.

However, there are clear grounds for optimism. Macroeconomic developments in the form of low inflation, fiscal consolidation, lower interest rates, and improving confidence levels and investment profitability are all creating the conditions for increased growth and employment.

While primary responsibility in the fight against unemployment rests with the Member States, the Union must support to the fullest extent their efforts to promote employment and minimise unemployment. In this regard, the European Council reaffirms its commitment to developing and deepening the integrated employment strategy, embracing macroeconomic policies and policies of structural reform, which it has developed since Essen and calls for it to be pursued with determination and consistency.

In its deliberations the European Council has endorsed the Joint Report on Employment of the Council and the Commission which has been prepared under the Essen strategy and has drawn on the Commission's first report on the initiative for "Action on Employment: A Confidence Pact". It has also taken account of President Chirac's Memorandum on a European Social Model.

In considering future action by the Union the European Council has also been mindful of the contribution of the Standing Committee on Employment and the outcome of the high level meeting of the Social Dialogue Committee in Dublin on 29 November.

It is necessary to continue with macroeconomic policies oriented towards stability, growth and employment. The European Council therefore endorses Member States efforts to achieve budgetary consolidation. There is no conflict between sound macroeconomic and budget policies on the one hand and strong and sustainable growth in output and employment on the other. The European Council emphasises that the selective restructuring of public expenditure should have a major role to play in promoting growth and employment especially through investment in human resources and active labour market policies. The positive impact of appropriate macroeconomic policies is enhanced where there is greater co-ordination of economic and structural policies as outlined in the Commission's report "Europe as an Economic Entity".

The commencement of Economic and Monetary Union (EMU) and the introduction of the euro in line with the provisions of the Treaty, will mean the creation of a zone of stability which will consolidate and strengthen the single market through the elimination of transaction costs and exchange rate risk for trade, tourism and investment among participating member States. EMU and the euro will make an important contribution to generating the stable macroeconomic framework necessary for sustainable employment.

To secure the maximum benefit in employment terms from the economic growth which can be anticipated in the period ahead, the European Council endorses the direction outlined in the Joint Report on Employment and the necessity to pursue, in accordance with national circumstances, policies of structural reform aimed at redressing deficiencies in Europe's labour markets and those in the Single Market for goods and services.

Labour market efficiency and investment in human resources need to be enhanced by:

- promoting life-long learning through incentives both for employers and workers;
- the development of a forceful human resources policy to meet the skills requirements of the new organisation of working life, driven by the new information and communication technologies;
- the creation of a labour market which is more open to employment through the increased responsiveness of individuals and enterprises to economic change;
- the modernisation of the organisation of work and increased mobility. To promote this, public policy should seek to combine worker protection with greater flexibility.

In this process, and particularly in the interests of equality, vulnerable groups - unemployed women, unemployed youth, the long-term unemployed - should be given particular support.

Member States are encouraged:

- with a view to promoting equal opportunities, to take the necessary steps to desegregate the labour market and to ensure that the high representation of women in part-time employment does not exclude them from training to enhance their future employability;
- to focus training and work experience on the particular needs of young people, to provide an effective response to the needs of early school leavers, and to consider means to encourage young people to take starter employment; the agreement between the social partners on the integration of the young in the field of work is particularly valuable;
- to take early action in a framework of active solidarity to prevent the unemployed drifting into long-term unemployment, in particular by supplementing training with individual counselling as necessary.

Taxation and social protection systems should be made more employment friendly.

The European Council stresses the importance for the Member States of creating a tax environment that stimulates enterprise and the creation of jobs as well as a more efficient

environment policy. More specifically, taxation and social protection systems need to be made more employment-friendly by:

- ensuring that these systems provide clear incentives for job seekers to take jobs or participate in other employment enhancing activities and for employers to hire more workers;
- developing social protection systems so that they not only provide unemployed people with a replacement income but also actively encourage participation in or preparation for work, so as better to promote reintegration and reduce dependence;
- developing social protection systems capable of adapting to new patterns of work and of providing appropriate social protection to people engaged in such work.

Efforts to modernise the markets for goods and services and exploit new sources of employment should be intensified by:

- speeding up implementation of outstanding internal market legislation so as to maximise the benefits of the Single Market;
- promoting the development of the services sector, with particular reference to Small and Medium-sized Enterprises (SMEs);
- exploiting new sources of employment. The fields of environmental protection and social services offer particularly promising prospects in this context.

European competitiveness should be advanced by:

- developing benchmarking as a tool for regular monitoring and evaluation of EU competitiveness against best world practice;
- striving to be at the forefront of the development of information and communication technologies, which are of crucial importance for employment and competitiveness; increased efforts are required of the Member States, the Council, the Commission and Industry to face the challenge of the Information Society;
- continuing the dialogue between Council and Commission in order to improve the effectiveness of state aid control and to reinforce control mechanisms;
- implementing the recently-agreed programmes for further improving the competitiveness of SMEs.

Local development should be promoted by:

- recognising the potential for stimulating employment growth, especially in new forms of work, targeting more effectively the needs of the unemployed and supporting the establishment and development of new businesses through vibrant local economies;
- securing the future of rural areas through a mobilisation of the entire rural economy;
- promoting an exchange of best practice and experience in this domain, and to report on the findings to the European Council at the end of 1997;
- mobilising the resources and contribution of all relevant actors, including public authorities and the social partners at local level. In this context, the European Council notes that many Member States have been developing the capacity of local communities

to participate actively in their own development and welcomes the positive reactions concerning the development of Territorial Employment Pacts, as proposed by the Commission.

Conclusion

The European Council urges Member States to continue with determination and consistency in their efforts to implement the Essen strategy and thereby to achieve a lasting improvement in the conditions for the generation of sustainable employment. At its meeting in December 1997 it intends to review again the implementation of this strategy. It anticipates that the Council and the Commission will in its Joint Report on that occasion attempt to identify the practices in Member States which have shown themselves to be most effective in implementing the strategy and to identify the remaining structural obstacles to reducing unemployment.

The European Council endorses the call in the paper on the Confidence Pact from the President of the Commission for a commitment by all the social and economic agents, including the national, regional and local authorities, the social partners and the Community institutions, fully to face their responsibilities in regard to employment within their respective spheres of activity. On the basis that their efforts are complementary, they should pursue a concerted drive to create the conditions necessary for employment.

ANNEX III

Declaration by the European Council on Former Yugoslavia

One year after the signing in Paris of the Peace Agreement for Bosnia and Herzegovina, the European Council welcomes the progress which has been achieved to date in its implementation, and in the broader peace process in former Yugoslavia. It pays tribute to the significant achievements of all the international organisations and agencies in Bosnia and Herzegovina in 1996.

The European Council fully endorses the outcome of the Ministerial meetings held in Paris (14 November 1996) and London (4-5 December 1996). It supports the Guiding Principles of the Civilian Consolidation Plan for a two year period as well as the detailed action plans, which elaborate the activities and obligations of the authorities of Bosnia and Herzegovina and of the international community for 1997. It attaches fundamental importance to the objective of having the authorities of Bosnia and Herzegovina taking the maximum responsibility for the country's affairs in the course of the consolidation period.

The European Council underlines the importance which it attaches to effective coordination of civilian aspects of implementation during the consolidation period and in this regard it reiterates the EU's strong support for the activities of the High Representative whose coordinating role has been strengthened for 1997. The early establishment of a formal relationship between the European Community Monitor Mission and the High Representative will represent a further practical demonstration of the Union's support for that office. The European Council also expresses its support for the continuing role of the OSCE, notably in supervising municipal elections in 1997 and in relation to the Royaumont Stability Process. It reaffirms its strong support for the International Criminal Tribunal and agrees that it will increase pressure on the authorities in Bosnia and Herzegovina and other states, particularly those which have failed to comply with arrest warrants issued by the Tribunal, to cooperate fully with the Tribunal, including by surrendering indictees.

Economic recovery and the return of refugees will be priority areas during the consolidation period. The EU is committed to continue to make a substantial contribution to the economic reconstruction effort throughout Bosnia and Herzegovina on condition that the authorities in Bosnia and Herzegovina themselves demonstrate their commitment to the reconstruction effort and comply fully with the provisions of the Peace Agreement. In this context, the European Council welcomes the plans of the European Commission and the World Bank for the convening of a further international Donors' Conference in early 1997.

The European Council emphasises the need to create and maintain conditions needed to encourage the return of refugees and displaced persons to places of their choice in Bosnia and Herzegovina. It welcomes the fact that the European Commission, the Office of the High Representative, UNHCR and IBRD, together with host countries and the authorities of Bosnia and Herzegovina, will work together to draw up and implement a coordinated plan to achieve this aim.

The EU's commitment to peace, reconciliation and stability in Bosnia and Herzegovina has been demonstrated in a very concrete and effective way through the efforts of the EU Administration of Mostar and the Office of the Special Envoy there. The European Council is satisfied that the primary objective of the EU Administration of Mostar - ensuring the establishment of a basis for a functioning unified local administration in the town - has now been met, and that the elected authorities there can now assume the main responsibility for the management of its affairs. However, many problems persist in Mostar, including continuing expulsions, harassment, intimidation and the influence of organised crime, and some local parties continue to obstruct political progress. The European Council calls on all parties to work together towards reconciliation. Recognising that there will be a continued need for an international presence to oversee implementation of the peace process in Mostar, and to consolidate political and economic achievements, within the framework of the overall peace implementation structures, it supports the decision of the High Representative to establish an office in the city.

The European Council recalls the EU's position regarding future relations between the Union and countries of former Yugoslavia. The development of these relations will be conditional upon full support for the Peace Agreement, including respect for Bosnia and Herzegovina as an independent, democratic, multi-ethnic State with secure borders, and upon full cooperation with

the International Criminal Tribunal, and, where applicable, upon full support for the Basic Agreement for Eastern Slavonia in Croatia. Respect for democratic norms and human and minority rights are key factors in the implementation of this approach. It recalls the intention of the Council to consider proposals from the European Commission, in the light of its ongoing discussions with the countries concerned for contractual relationships in the context of the Union's regional approach.

The European Council recalls the terms of Presidency Declarations of 22 November 1996 concerning actions by certain authorities in Croatia and the Federal Republic of Yugoslavia which, in the Union's view, work against the objective of progress towards democracy. In both countries, the situation of the independent media remains a source of concern.

The European Council recalls the Council's conclusions of 6 December 1996 condemning the annulment of certain election results in the FRY. It notes that serious tensions persist and urges the Belgrade authorities to demonstrate full respect for human and minority rights and the observance of democratic norms, especially with regard to the electoral process. In this context, the European Council notes with interest Belgrade's invitation to the OSCE to send a delegation to investigate the facts of the recent local elections. The OSCE may wish to consider the conditions for such a mission, notably in relation to the right to recommend a reversal of the annulments or a rerun of some elections. The European Council attaches importance to dialogue among all political forces with a right to be represented in parliament in order to establish rules to govern elections in 1997. It calls on all parties to show restraint, refrain from the use of force and promote dialogue. Respect for human and minority rights and democratic norms will be key factors in determining the Union's future relationship with that country and its further integration into the international community. The European Council also recalls the conditions set out in the Presidency's Declaration of 9 April 1996 on relations with the Federal Republic of Yugoslavia, including the need for the granting of a large degree of autonomy to Kosovo within the Federal Republic of Yugoslavia.

The Council takes note of the current situation regarding implementation of the Basic Agreement for Eastern Slavonia in Croatia and reaffirms its full support for the efforts of the UN Transitional Administrator and his staff. The EU will continue to support the economic rehabilitation and reconstruction of Eastern Slavonia. It calls on the Croatian Government and the local Serb leadership to cooperate fully to ensure full implementation of the Agreement in 1997.

ANNEX IV

Declaration by the European Council on the Middle East peace process

1. The European Council expresses support for the Special Envoy to the Middle East Peace Process and welcomes the declared willingness of all parties to cooperate with him. It calls on all parties to recognise his appointment as a further demonstration of the Union's commitment to promoting peace in the Middle East.
2. Recalling its Declaration at Florence on 21 June and the Council's Declaration at Luxembourg on 1 October, it reaffirms its support for the fundamental principles of a just and lasting settlement in the Middle East, notably land for peace and self-determination for the Palestinians, with all that this implies.
3. The European Council is gravely concerned by the continuing deterioration in the peace process. It calls on all parties actively to discourage violence and work for a reduction of tension so that negotiations can resume on all tracks in accordance with the principles of Madrid and the terms of the Declaration of Principles.
4. The European Council calls for an early resolution of the deadlock over Hebron, implementation of the other outstanding elements of the Interim Agreements, and the early resumption of the Permanent Status Negotiations.
5. The settlements issue is eroding confidence in the peace process. Settlements contravene international law and are a major obstacle to peace.
6. Palestinian social and economic development require the immediate lifting of the blockade. The European Council urges the Israeli authorities to remove all restrictions except where Israel's legitimate security interests are manifestly engaged, as in the case of acts of terrorism. The dire economic consequences- with their effect of breeding discontent and violence- have dissipated the optimism generated by the establishment of Palestinian self-rule. The Council has instructed the Special Envoy to promote concrete and immediate measures to address these issues.
7. The European Council urges the Government of Israel and the Palestinian Authorities to cooperate at all levels in the interests of security and to take all necessary measures to control extremists and combat terrorism.
8. In the spirit of the Barcelona Process the European Council calls on all Mediterranean partners which are concluding Euro-Mediterranean Association Agreements, to join with the Union in a common effort to advance the development and integration of the Palestinian economy within the region. The European Council recalls that both the Association Agreement with the Palestinian Authority and the similar Agreement with Israel commit the parties to promote compliance with the basic norms of democracy, including respect for human rights and the rule of law.

NOTES

1. The contents of this report are subject to Parliamentary reservations.

[2.](#) A first assessment by the Council according to Treaty Article (EC) 109 j (2) has taken place, and the Council recommends its finding to the Council meeting in the composition of the Heads of State or Government; see Annex 1 to this paper.

[3.](#) Under Article 5 of Protocol 11, this obligation does not apply to the United Kingdom unless it notifies the Council that it intends to move to the third stage.

[4.](#) See "Conclusions of the Presidency on the European Council in Florence of 21 and 22 June 1996" (SN 300/96), including the attached "Progress report by the ECOFIN Council to the European Council on preparation for Stage Three of EMU" (7940/96), dated 4 June 1996.

[5.](#) "Monetary and exchange rate policy cooperation between the euro area and other EU countries". Report to the Informal ECOFIN Council session in Dublin on 20-22 September 1996, dated 3 September 1996.

[6.](#) For the sake of simplicity, EU currencies and EU countries outside the euro area which participate in the new exchange rate mechanism are hereafter referred to as "non-euro area currencies" and "non-euro area Member States", respectively; the respective NCBs are referred to as "non-euro area NCBs".

[7.](#) Cf. Article 109c(4).

[8.](#) Cf. Article 44 of the Statute of the ESCB/ECB in combination with Article 4.1 of the Statute of the EMI.