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The Question of European
Reparations in Allied Policy,
1943—1947

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Preface

The question of reparations has usually been associated with Germany. Disappointing experiences after the First World War and the reconstruction of Germany after the Second World War have been the object of several studies. In some of these interpretations, especially those according to revisionist theories, economic factors play an important role in explaining the origins of the Cold War. It has been argued, for example, that the United States neglected to come to a formal decision on German reparations and thus forced the Soviet Union into the Cold War.

It has not been my intention so much to examine the roots of the Cold War, as to attempt to explain how the question of reparations after the Second World War related not only to Germany, but also to all the European countries associated with her. I have left countries like Japan, which were in a different political situation, outside my study.

I wish to express my special thanks to Tuomo Polvinen and Erkki Pihkala, who have contributed significantly to the writing of my research. Marjatta and Robert Bell read and improved my first draft. I am very much indebted to Hal Martin for translating my manuscript into English. I would also like to thank the Finnish Historical Society for including my study in its series, and to Rauno Endén for editorial assistance. I am also grateful for the grant I received from Commission for the Promotion of Finnish Literature.

Hannu Heikkilä

Reparations as Part of Allied Policy

Legacy of Earlier Reparations

As long as wars have been waged, victors have exacted satisfaction from losers in one form or another. In addition to defeat the losing side has been burdened with the delivery of booty and reparations. Payments have consisted of transfers of national property such as machines and ships, or of items of the national income — "current production". Originally transfers of goods were the only means of payment, but as money became current it was largely used instead. After her defeat in the war of 1870—1871, for instance, France paid Germany five milliard francs in gold.

The best-known reparations are undoubtedly those enjoined on Germany after the First World War. They were paid partly in money and partly in kind, mainly the former. These money payments caused serious problems. Leaving the precise sum unmentioned, the Versailles Treaty obliged Germany to compensate for all damage caused to civilians, losses arising from ill-treatment of war prisoners and destruction of non-military property; she was also obliged to pay pensions to war veterans.

In the years following the war efforts were made to place an obligation on Germany which should be practical and acceptable to all parties concerned. This resulted in a many-phased tangle of events which contributed to the economic uncertainty of the 1920s. When Adolf Hitler came to power in Germany the Third Reich refused to recognize all the important political and economic injunctions of the peace treaty.

The grand total paid by Germany cannot be particularized. On reparations discharged from 1918 to 1924 there are no undisputed

data, and in the estimates of goods deliveries there are great differences. According to a delegation appointed by the creditors Germany paid some 21.8 billion marks, while the Germans themselves claimed to have paid 67.7 billion. The most reliable calculations made by investigators suggest a sum of about 30 billion. At the time concerned, however, Germany borrowed some three milliard marks from abroad. This matter — the financing of reparations — was a central factor during and after the Second World War when the Allies considered their attitude to reparations.

Various reasons have been advanced for the failure of the reparations article in the Versailles Treaty. Some investigators have stressed that the economic effects of the reparations concerned were in fact quite small. The main reason was the unstable political situation in Germany and the unwillingness of her people to accept responsibility for the war. For their part the creditors were not prepared to accept reparations in the practical form of goods, but demanded most of them in money. It has been stressed on the other hand that the obligation imposed on Germany was beyond her capacity to pay. For the reparations programme to succeed, it would have been necessary after the war for Germany to expand her industry vigorously and secure a large export income.¹

Mistakes in the peace treaty of the First World War cast a dark shadow over plans for peace after the Second World War. The Versailles Treaty had laid a foundation for the arms race, economic depression, nationalism and many other factors affecting international relations. For Britain, the Soviet Union and the United States, therefore, the central lesson of the first war was that Germany must be watched more effectively than in the 1920s and 30s. The conclusion to be drawn from the relevant article of the Versailles Treaty was that reparations — which there was no need to abandon altogether — must be exacted more skilfully than before. The views of those engaged in the war differed, however, as to how mistakes should be avoided.

1) Dillard 1967, pp. 512—515, 517—519; Röper 1964 and sources mentioned; Taylor 1976, pp. 69—76.

War Aims

Allied war aims were expressed — very loosely — in the Atlantic Charter (12.8.1941) and the Declaration of the United Nations (2.1.1942). Both emphasized certain general principles such as just treatment of the defeated, but such a particular item as reparations was not defined in any way. Later too reparations were briefly passed over when Allied political leaders met — as when Eden, Britain's Foreign Secretary, visited Moscow in December 1941.²

In the Atlantic Charter President Franklin D. Roosevelt and Prime Minister Winston Churchill repudiated territorial changes except where "freely declared" by the nations, and pledged themselves to self-determination and disarmament. This was not an adequate basis for peace, however, as economic questions and peace were closely connected. By the terms of the Charter Britain and the United States wished, on the strength of obligations then in force, to promote the access of great and small powers, victors and vanquished alike, to trade and the world's raw materials on an equal basis. There should be maximum collaboration between all countries in the economic field, so that all might be assured of a better living standard, economic progress and social security.³

In the phraseology of the Atlantic Charter the "open door" policy of the United States was clearly reflected. International peace was based on economic welfare. World welfare and therefore peace could be achieved only by means of "healthy" world trade. This in turn implied open doors to markets. The United States fully realized that the world economy depended on the American contribution, but world trade would also guarantee the welfare of the United States. Reparations were seen in this context: they must not disturb international trade or otherwise oppose American interests. The Americans did not intend to be the financiers of reparations.

The United States took the Atlantic Charter as the basis of their policy according to which decisions concerning peace were to be

2) Feis 1974, pp. 20—23; Joyce and Gabriel Kolko 1972, pp. 11—15; Paterson 1975, pp. 3—8; Wheeler-Bennet-Nicholls 1972, pp. 36—43; Woodward 1962, pp. 203—210, 220—243.

3) Wheeler-Bennet-Nicholls 1972, pp. 43—44.

left until the peace conference following the end of hostilities. In September 1941 with some reservations the Soviet Union approved the Atlantic Charter despite the fact that she had not been consulted over its form of words. But Stalin desired final decisions while the war was still going on, and in Moscow the policy of delay aroused evident suspicion of a united front of capitalist nations against the Soviet Union. It was of the first importance to bring the war to a conclusion as soon as possible, so that destruction and suffering in the Soviet Union should be reduced to a minimum. This aim would have been effectively served by the opening of a second front in the west.

The British hoped the Atlantic Charter meant that the United States would come into the war as soon as possible and assume part of its burdens, and that the Americans would also engage in planning the postwar settlement. In that case the United States — unlike their policy after the First World War — would not give aid without defined conditions. American funds should rather be directed more to Britain and the Soviet Union than to Germany and her former allies.⁴

Preliminary Attitudes and Plans

The above declarations and talks remained of a general nature, but the Allied administrative authorities continued to work towards a decision on reparations. The latter were linked with restrictions intended to prevent German rearmament when peace returned. Less reserved in their attitude to reparations were the Soviet representatives, whose views became known at the time of a conference of foreign ministers in Moscow (19—30.10.1943) in the form of an article by Academician Evgeni Varga.⁵ Other examples of a similar attitude appeared in the Soviet Union during the war. To the Soviet reparations were not only a question of security, but emphatically one of justice also: on the one hand Germany and her allies, as aggressors, were obliged to make good the destruction they had caused; on the other, the Soviet Union was entitled to the

4) Woodward 1971, pp. 203—210.

5) Varga, 1943. Maisky 1967, p. 383. Mastny 1979, p. 111.

main part of the compensation. Reparations should also ensure that the living standard of the aggressors should not rise above that of the victims. Thus reparations would help the carrying out of the five-year plan whose aims the war seemed to have moved far into the future.

According to Varga Germany was able to pay only a small part of the coming reparations from property held by her abroad or from her national assets, and the main stress was therefore on her national income or current production. From 1924 to 1929 compensation paid by Germany amounted to only 1 1/2—4 % of her national income, while 10 % went on capital investments and growth of the military potential. Only part of the funds obtained in foreign loans was applied to reparations, and part of the benefit went to German economic life. Germany in fact could have paid reparations, but mistakes had led to these not being carried out.

There was a failure also on the part of the creditors themselves, their receiving capacity being inadequate to cope with Germany's productive capacity. In the light of experience after the First World War there seemed good reason to demand payment in kind, which Varga expected to be advantageous to a planned economy like that of the Soviet Union. With adequate supervision and planning the payment of reparations would be quite possible.

As Germany was not able in practice to make good all the destruction caused, it was Varga's view that making good material damage should take priority. The total sum to be claimed should be divided among the states concerned in proportion to the loss inflicted on their national assets — not the destruction suffered in absolute terms. Without giving an estimate of the Soviet share Varga stressed that the destruction suffered by his country was such that she was entitled to the main part of the compensation. Varga's article actually dealt with Germany, but he also stressed the obligation of Italy, Rumania, Hungary and Finland.

Destruction caused by the Germans in Britain caused the British also to consider demands for reparations. Bearing in mind the lesson learnt after the First World War, Germany must also be prevented from becoming more powerful than Britain in trade.⁶

6) *Reparations. Memorandum by the President of the Board of Trade* (Dalton), 28.8.42 Public Record Office = PRO FO371 31514 U767/27/70.

And there were many British critics of the Versailles decision on reparations — most conspicuously Lord Keynes, who during the Second World War exerted a profound influence on the economic decisions of His Majesty's Government.⁷

The attitudes adopted to reparations led to the appointment of a committee composed of representatives of various ministries. This committee, which was known by the name of its chairman Sir William Malkin, legal adviser to the Foreign Office, reported in August 1943.⁸ It took note of Germany's obligations, but considered that it was not practical for all the destruction to be made good. Germany's economic resources together with the provisions of the Atlantic Charter and the statements of political leaders imposed limits on possible demands. The committee recommended that actual reparations liabilities should be discharged within five years from the appointment of a commission to be set up for this specific purpose. Goods offered as reparations were to be supplied from stocks existing at the time the armistice was concluded as well as from current production.

At the end of September a ministerial conference proposed by Foreign Secretary Eden was held, and at it ministers concerned with reparations tried to find a united line. The Malkin committee's report was received with reservations. The Cabinet had not yet decided, for instance, whether Britain desired the division of Germany and the dismantling of her industry, whereas the Malkin committee had started from the notion of a unified Germany with its own industrial capacity. A conclusion on the British line was not reached, but the views expressed in London were passed on to Washington.⁹ On the basis of the Malkin report Keynes explained to Dean Acheson, W. Averell Harriman and

7) FO Minute (Ronald) 13.11.1941 FO371 28907 W13570/426/49 PRO. *Compensation to be required from the enemy.* (s.d.) FO 371 28908 W13983/426/49 PRO, *Germany's Control over Economic, Industrial and Commercial Organization. The question of Restitution and Release. Memorandum by the Department of Overseas Trade* 11.7.1942, FO 371 35305 U4456/6/70 PRO. Einzig, 1942.

8) *Report of the Interdepartmental Committee on Reparation and Economic Security* 31.8.1943, FO 371 35305 U4059/6/70 PRO. Cairncross 1986, pp. 19—33.

9) Lae (Washington) to FO 16.9.1943, FO371 35309 U4409/6/70 PRO. Keynes (Washington) to FO 29.9.1943, FO371 35309 U4973/6/70 PRO.

others that in Britain's view the "false conclusion" should be avoided that all attempts to obtain reparations were useless.¹⁰

The Malkin report showed that of the British were prepared to use reparations as a principal means of supervision in postwar Germany. In the end this question became part of a wider regulation of the German settlement in which several interconnected factors had to be taken into account. When, for instance, occupation of Germany appeared to be an alternative worth considering, the British also needed to take into account the economic and social state of the area to be occupied. There was no reason for them to incur trouble in the form of social unrest arising from poor economic conditions.

Given Britain's past experience of them and their possible role as an alternative in peacetime planning, reparations were a far more meaningful matter to the British than to the Americans. In the United States reparations were thought of as a problem related to the aftermath of the First World War and a problem most easily solved by being ignored. The enemy had never penetrated United States territory in such a way as to cause a demand for reparations. Interest in the subject did not grow until 1944, when several committees studied it in Washington. Plans generally contained proposals for payment in the form of current production, which would have fitted into the economic relations inherent in the open door policy. German goods received without payment could have helped in the reconstruction of the rest of Europe, and thus might have lessened the need for American credits. Although German needs would be subordinated to those of the rest of Europe immediately after the war — there would be no transfers of national assets — the Germans would still retain sufficient industrial resources to engage later in economic relations without restraint. But before reparations were imposed on the Germans a reasonable living standard had to be guaranteed.¹¹

Larger reparations could be obtained from Germany if she were first allowed to recover from the war. In that case, however, the creditors would not have obtained the extra contributions they most urgently needed for reconstruction. Reparations received

10) Backer 1978, pp. 29—30.

11) Kuklick 1972, pp. 43—44.

later might weaken the open door system. In Washington, admittedly, opposite viewpoints were also presented. Henry Morgenthau, Secretary of the Treasury, eventually proposed that German industrial capacity be dismantled and the country turned into a mainly agricultural state. His idea was not approved. Although no final decision was made in Washington on reparations, a substantial German contribution to European reconstruction was generally expected. Optimism was increased by the notion that international reconstruction and the ideas making up the open door policy would be quickly realized when the war ended.¹²

Talks Begin

Reparations became a subject of Allied discussion in October 1943 at a conference of foreign ministers in Moscow; this was mainly concerned with military matters, the Soviet Union wishing to be assured that a second front would be opened in northern France. On 29th October reparations were briefly dealt with on the basis of a report submitted by Secretary of State Cordell Hull.¹³ This treated the matter at a general level as part of European reconstruction. Limitations were proposed which were against the principles expressed by the Soviet Union: as a rule reparations would be demanded not in money but in goods and services, the receiving country must approve them, third countries must not suffer harm and German productive activity must not be exposed to disturbances causing economic and political problems.

The dissatisfaction of Soviet Commissar for Foreign Affairs V.M. Molotov with Hull's proposal came as no surprise. Molotov also criticised it for dealing only with Germany and forgetting the latter's allies. Moreover more concern seemed to be shown for Germany's living standard than for the subsistence of the Soviet

12) Gaddis 1972, pp. 118—121. Kuklick 1972, pp. 69—73.

13) Conference Document No. 39. U.S. Proposal with regard to Questions of Reparations, Foreign Relations of the United States (=FRUS) 1943 I, pp. 740—741.

people. The Soviet Union was not in a position to make a counter-proposal, however, having received Hull's proposal only on 25th October. It was easy for Eden to agree with Hull's principles, which took into account Britain's views expressed in Washington. The Foreign Office estimated that Hull's proposal provided a basis for proceeding to details, which could be done within the German reparations commission which the proposal suggested.¹⁴

The Moscow conference made no further progress in the matter of reparations. Allied political leaders were obviously unwilling to analyze differences of opinion over the postwar settlement which might weaken the collaboration of primary importance.

Relying on Hull's memoirs, *Clemens* maintains that "Hull's recommendations became the kernel of the Soviet reparations program as constructed and presented at Yalta by Ivan Maisky." As will appear later, the Soviet proposal at Yalta was nearer to the principles expressed before Hull by Varga. Molotov's qualified approach to the American proposal was based on real differences of view on reparations themselves. Yet the conclusion reached by Clemens shows how near to each other the views of the great powers on reparations were at this point.¹⁵

The Moscow conference was important in strengthening collaboration between the three powers concerned. Their decisions endorsed the principle that preliminary peace feelers should be conducted by the Allied power which had been principally engaged in war against the country concerned. Thus Britain and the United States would concern themselves with Italy, the Soviet Union with Bulgaria, Rumania, Finland and Hungary.¹⁶

German reparations were not discussed at the Teheran "Big Three" conference of November-December 1943. But the matter went to the European Advisory Commission set up in Moscow whose task was to prepare the surrender terms to be presented to Germany. The Commission held its first official meeting on 14th January 1944. In July 1944 it produced a draft document of surrender and by September a plan for the occupation of Germany.

14) FO Minute (Coulson) 17.11.1943, FO371 35309 U5932/6/70 PRO.

15) Clemens 1970, p. 38 and sources mentioned. Cairncross 1986, p. 62.

16) Feis 1974, pp. 206—223.

In all the Commission submitted 12 agreements for Allied approval, but several which were concerned with the status of Europe and above all Germany remained unapproved amid the deepening disagreements of the great powers. Among the matters they dealt with was that of German reparations, about which the next phase of discussion was to take place at the Yalta conference.

Teheran: Finland

Although no progress was made at Teheran on reparations with regard to Germany, the question arose in another connection. This was in discussion of the status of Finland, which had been a concern of great power policy during the preceding months.

During the spring of 1943 peace feelers in the direction of Finland were being made on a more promising basis now that the war was beginning to turn in favour of the Allies, especially after the battle of Stalingrad and the raising of the Leningrad siege. Having obtained Soviet approval, the United States decided to make its good offices available for the arrangement of peace negotiations between the Soviet Union and Finland. In March 1943 Molotov communicated to the United States — but not to Finland — the "minimum conditions", one of which was that at least 50 % of the total damage inflicted by Finland on the Soviet Union during the war be made good.¹⁷

Thus a reparations article was included in the Soviet Union's first outline of peace terms. And so at this stage — several months before the Moscow foreign ministers' conference — the principle emerged that a reparations article should be included to the peace terms applied to states which had fought beside Germany. However, to make good all destruction would have been too great an undertaking, and the Soviet Union accordingly declared itself satisfied with partial compensation.

In accordance with a pact of alliance made in May 1942 Stalin informed Churchill of this. The latter doubted the willingness of the Finns to withdraw from the war because they were dependent on German grain deliveries, but he left the matter to Stalin. Later

17) Polvinen 1979, pp. 142—215, and 1986, pp. 5—9. Berry 1987, pp. 264—288.

the Soviet ambassador in London, Ivan Maisky, responded that the Kremlin was not seriously anxious over the handling of this question, but was prepared to announce its minimum terms. To Maisky Churchill commented only on the last item, which dealt with reparations. Maisky said that the Soviet Union had thought of accepting certain goods it needed, such as wood and paper, for reparations, rather than money. Churchill advised Maisky not to insist on the reparation terms but to lay stress on the acquisition of materials needed by the Soviet Union.

It is probable that Churchill's statement was based on his own conclusions concerning the consequences of reparations after the First World War. By March 1943 the plans made in London for German reparations were no more than preliminary ones, and no complete set of terms to be imposed on Finland had been worked out, not even with regard to reparations. Securing timber for Britain was hardly an issue, for Churchill had no wish to oppose the Soviet demand for Finnish timber and paper as such. Churchill wished the Soviet Union to know, however, that he opposed reparations though he did not believe that the United States' proposal for mediation would lead to practical results.

One reason for Churchill's negative attitude to the reparations article was that the Allies had not yet reached an understanding on the principles of reparation. This article could become a precedent within a broader set of arrangements on which Churchill thought the Allies should come to an agreement before finding a solution for Finland.¹⁸

The Soviet peace terms disappointed Washington, for the Americans did not believe that the Finns would accept them. The United States gave up its attempt at mediation to the surprise of the Finns, who were ignorant of the Soviet terms. In spring 1943 Finland's peace efforts came to nought when contacts made through Sweden and Britain also brought no results.

The first move toward an armistice with Finland was made by the Kremlin in November 1943. The Soviet ambassador in Stockholm, Mrs Aleksandra Kollontay, asked Erik Boheman,

18) W.M (43) 46th Conclusions Minute 3. Confidential Annex 29.3.1943, Cab 65—37 PRO. Churchill to Maisky 31.3.1943 FO copy, FO371 36838 N2610/37/56 PRO.



Winston Churchill, Britain's Prime Minister, at his desk in No. 10 Downing Street. In his opinion "the Finns might fell a tree or two", but no great benefit would result.

secretary-general of the Swedish Foreign Ministry, to inform the Finns that their representatives would be welcome in Moscow to discuss peace. Stalin received the Finnish answer, which expressed a willingness to negotiate, while attending the Teheran conference of the three great powers. On 1st December he outlined to Roosevelt and Churchill the feelers which had been put out and expressed the opinion that Finland's reply showed a lack of real desire for peace.

At this point Churchill intervened actively on the question of Finnish reparations. In his opinion "the Finns might fell a tree or two", but no great benefit would result. Stalin totally disagreed. He did not desire money, but believed the Finns capable of making good the destruction they had caused within 5—8 years by supplying paper, timber and other goods to the Soviet Union. Finland must be taught a lesson, and Stalin was determined to obtain satisfaction.

Churchill surmised that the destruction caused by Finland was clearly more than an indigent country could make good. But the discussion ended with Stalin presenting a compressed version of the Soviet demands, one of which was for 50 per cent compensation for damage caused by the Finns. Churchill still tried to induce Stalin to renounce the reparations article, but the latter declared his readiness even to occupy part of Finland as a guarantee of payment. If the Finns paid, Soviet troops would withdraw from the area concerned within a year.¹⁹

Apart from the reparations question the western powers were satisfied with the Soviet peace terms and willingness to negotiate, which was welcomed. In accordance with agreed Allied policy the conclusion of peace was a matter between the Soviet Union and Finland on which, it was believed in London and Washington, no influence at all could be exerted. At this stage Finland's army was still deep in Soviet territory, and the country's government did not believe that public opinion would be likely to accept peace on Soviet terms.

At Teheran Stalin demonstrated to the Allies that a peace treaty could not be concluded without a reparations article. Deliveries must be in the form of goods — he mentioned paper and wood as examples — over a period of 5—8 years. They should amount to 50 % of the damage caused by the Finns — he did not specify value or quantity. Also at this stage no prices were fixed for the goods concerned. Churchill rejected the whole possibility of reparations and was therefore unwilling to go into detail.

Peace Feelers, Spring 1944

Peace feelers initiated by the Soviet Union gathered speed when the western Allies and Sweden began urging Finland to make a separate peace. Further pressure came in the form of Soviet bombing attacks on Helsinki at ten-day intervals during February. Finland's government yielded to the extent of asking to hear the Soviet peace terms, which were also communicated to the Allies,

19) Polvinen 1979, pp. 286—293. Fischer 1968, pp. 78—80. Kennan 1960, pp. 34—36.

though Stalin expected the British to stand aside from the actual negotiations. Among the terms it was stated that reparations should be discussed in Moscow. The British view was that the terms were a good starting-point for negotiations after the adjustment of a few details. As the Foreign Office saw matters, Britain was entitled to intervene with regard to all the peace terms — reparations included.

On 20th March Eden was able to inform the War Cabinet that the Soviet government had consented to the arrival of Finnish representatives in Moscow, where they would be given an interpretation of the terms without preconditions. At the end of the same month Finland's representatives reached Moscow, where much of the substance of the articles was explained in detail. Molotov also made the Finns understand that no agreement could be reached without a reparations article. This has sometimes been taken to mean that Soviet demands had grown stricter since the terms stated in Stockholm. It had then been promised that reparations might be a matter for discussion, but Molotov's statement in Moscow was regarded as ruling this out.

As long as Soviet archives remain closed this question cannot be finally resolved, but the available material does not point to so extreme an interpretation. To its Allies the Soviet had expressed a firm intention to demand reparations from Germany and her allies, and an article in some form respecting this was accordingly a minimum Soviet demand. The Soviet attitude clearly signified, on the other hand, that the substance of the article could have been discussed in Moscow.

While Molotov stressed damage caused by Finland especially in Leningrad and the Murmansk area, the Finns understandably drew attention to the destruction suffered by Finland and to the cost of reconstruction in Karelia. According to Molotov destruction caused by the Finns amounted to 1,200 million dollars, of which they would be required to provide half ie. 600 million dollars in the course of five years. Reparations would be paid in goods such as ships, paper, pulp and machinery. Finnish sources make it clear that Molotov required prices to be fixed at current market value.²⁰

20) Palm 1971, pp. 90—95. Palm 1973, pp. 73—74, 80—82.

Regardless of the course followed by the Moscow negotiations some attention must be paid here to Finnish views on reparations in connection with the Soviet demand. To the Finns the war had been a defence of their own independence — as the country's political leaders strove to indicate. Both sides suffered losses, and the Finns did not feel that they had caused exceptional destruction to the enemy. Finnish air activity, for instance, was limited to actual battles: there were no resources for bombing enemy population centres. The Finnish government instructed its representatives to say that payment of reparations could not be regarded as reasonable.

In the view of Finland's political leaders, however, the question was not merely one of justification. In the foreground was a mistrust of Soviet aims. Whatever their amount, reparations were seen as leading to a situation in which the Soviet Union would be able to supervise Finland's economic life. This view is well expressed in a letter of mid-April 1944 from Finnish Foreign Minister Ramsay to the Ambassador in Stockholm, G.A. Gripenberg. In it he states that the actual amount of the reparations was not ultimately important. "600 or 450 million dollars will lead to exactly the same result: supervision of Finnish production and a lowering of our living standard."²¹

Finland's answer to the Soviet Union was that the latter's terms were impossible to fulfil. They shook the foundations of independence and imposed an excessive burden on the national economy. This answer aimed on the one hand at avoiding a detailed discussion of the terms which might lead to a fruitless argument; on the other it closed the way to further negotiations. Both parties understandably tried to place the blame on each other, and the Finnish aim was to take advantage of all statements asserting the harmfulness of reparations.

Both in Stockholm and in London the Soviet reparation demand was regarded as exceeding Finland's productive capacity, though it was privately estimated at the State Department that the obligation could be carried out.²² In London the situation was easy

21) Ramsay to Gripenberg 14.4.1944, Gripenberg Papers, file 4 VA.

22) Lundestad 1978, p. 288. *Finland's Capacity to pay the Russian Reparations Demand* 24.6.1944, RG59 R&A Report No. 2127 NA.

to follow because the Soviet Union informed its Allies well before Finland's answer was given. On 1st April the new Soviet Ambassador in London, F.T. Gusev, went to inform the Foreign Office of the negotiations which had been carried out. Under-Secretary of State, Sir Orme Sargent, observed on that occasion that the British might intervene over the reparations article, though the terms otherwise were reasonable. The Foreign Office learned that Sweden too opposed the Soviet reparations demand.²³

In a reply note prepared by Britain a few days later the reparations question was taken up. A sum of 600 million dollars was considered too large for Finland's capacity, and such a demand might bring the whole of the peace negotiations to nought. Accordingly a reduction of the sum was recommended. Apart from Finland's capacity to deliver, the interests of Britain herself were noted in this reply. It was felt that Finnish reparations could not be provided from British property.

The Foreign Office calculated that 600 million dollars signified 75—100 % of all Finnish export for the following five years. Britain was interested in obtaining timber, pulp and paper for her own reconstruction, and Finland was an important source. The British reply did not go further, however, in exerting pressure on the Soviet Union, who might declare its own ability to sell Britain the materials she required. This alternative in all probability would have meant higher prices for Britain.²⁴

British Interests

While Finland was still considering her answer Churchill on 4th April brought up the Finnish question in the War Cabinet. He stated that the reparations demand in itself must be considered too large, but Britain's interests in Finland should also not be forgotten. In Churchill's view these interests now came to the fore in discussion of Finnish reparations. He observed at the same time

23) FO Minute (Sargent) 2.4.1944, FO371 43160 N1968/30/56 PRO. Mallet from Stockholm to FO 2.4.1944, FO371 43160 N1990/30/56 PRO.

24) Great Britain's reply note to the Soviet Union 4.4.1944, FO371 43160 N2047/30/56 PRO. FO Minute (Warner) 4.4.1944, FO371 43160 N2047/30/56 PRO.

that if this was the only obstacle to peace with Finland it would be in the Finnish interest to make a treaty with the Soviet Union even on heavy terms in the hope that reparations would be reconsidered at the peace conference as part of a general agreement with the Soviet Union.²⁵

Churchill took the Soviet demand as a starting-point on which further negotiations might be held later even if the Finns accepted it in principle. As will be shown more precisely later, the Finns were given some relief when their obligation was reduced to 300 million dollars. This was not the result of negotiations between the Allies or between Finland and the Soviet Union, but was decided by the latter unilaterally.

On the same day (11th April) as the Cabinet dealt with the Finnish question Great Britain's Ambassador in Moscow, Archibald Clark Kerr, obtained by letter further information on the Soviet peace terms at the Foreign Office's request. London wished to know what goods the Soviet Union desired to receive from Finland and on what basis it had arrived at its demand for 600 million dollars. Britain was unable to particularize her own demands until this information was received from the Soviet. In this connection London stressed its wish to secure deliveries to Britain of timber, pulp and paper. Clark Kerr's letter further stressed that the above materials must not reach the enemy by way of neutral countries. In any armistice or peace treaty the Finnish government should be obliged to export all such material which were not intended for the Soviet Union to other members of the United Nations.²⁶

Churchill was also prepared to act with a view to reducing Finnish reparations. Without knowing of the action taken by the Foreign Office he inquired of the Permanent Secretary, Sir Alexander Cadogan, on 12th April 1944 how a revision of reparation terms for Finland and Rumania might be suggested to Molotov in view of the world economic situation at that time. Reminding Cadogan of what happened after the First World War Churchill forecast that the Soviet Union was unlikely to get much

25) W.M. (44) 47th Conclusions Minute 2. Confidential Annex 11.4.1944, Cab 65—46 PRO.

26) Clark Kerr to Vyshinsky 11.4.1944, FO371 43160 N2814/30/56 PRO.

out of the countries concerned.²⁷ Following the British note to the Soviet Union on 4th April the Kremlin had given no answer, and for this reason Churchill thought it expedient to send Clark Kerr instructions on 15th April suggesting the above-mentioned revision.²⁸ Thus Clark Kerr received instructions to take steps which he had already taken by order of the Foreign Office.

Finnish reparations were a potential source of friction in Anglo-Soviet relations, but they did not become so on account of the answer given by Finland. In Western Allied circles the Finns were expected to make clear that the reparations demand was beyond the country's productive capacity. But the Finnish statement gave grounds for considering that the Soviet proposals in their entirety — not merely with regard to reparations — had been rejected, as Churchill noted at the Cabinet meeting.²⁹ In London it was thus possible to conclude that at this stage the British were no longer needed: the next move was for the Soviet Union alone. If it had been a question of reparations only, the Foreign Office would probably have intervened in the reply to be given to Finland, as was pointed out in a note conveyed to Gusev. What this would have meant in practice was a matter to occupy the Soviets, and the records shed no light on it.³⁰

In both London and Stockholm there was a strong impression that a different answer would have enabled Finland to proceed to further negotiations on the reparations article and thus — partly with the support of Western opinion — to obtain easier terms for an armistice or at least for a final peace treaty. Stockholm had information that the Kremlin was willing to discuss the matter, but the Finns had acted "with their typical diplomatic stupidity."

By the answer they gave, Finland's political leaders avoided a situation which the British and Swedes hoped they would reach: engagement in negotiations which would lead to easier reparation terms. It should be noted, however, that reparations were made by no means the only obstacle in the way of peace. Removal of

27) Churchill to Cadogan 12.4.1944, Prem 3 170/3 PRO.

28) Cadogan to Churchill 14.4.1944 and Churchill to Clark Kerr in Moscow 15.4.1944, Prem 3 170/3 PRO.

29) W.M. (44) 53rd Conclusionc Minute 1. Confidential Annex 20.4.1944, Cab 65—46 PRO.

30) FO to Clark Kerr in Moscow 22.4.1944, FO371 43160 N2441/30/56 PRO.

German troops from the country and territorial questions were also impediments to a mutual understanding. In this connection it is pointless to calculate whether Finland would have obtained other concessions than these over the reparations article. Finland's political leaders took the view that the terms as a whole were too severe to form a foundation for peace.

When the peace feelers led to nothing the Soviets did not find it necessary to explain the principles behind the reparations liability they had insisted upon. Inquiries made by Clark Kerr throughout the summer were answered repeatedly with the reply that the Finnish question was not of current interest.³¹

31) FO Minute (Nutting) 17.8.1944, FO371 43163 N4913/30/56 PRO.

The First Treaties

Peace Feelers in Relation to Rumania

During the spring of 1944 the question of an armistice with Rumania also arose. The Allied aim was to detach Rumania from the war as soon as possible, and peace feelers were put out by the Rumanians from the early part of 1944 onwards. The Red Army advanced into Rumanian territory at the beginning of April 1944, and soon after this the Soviet Union gave its terms for an armistice.³² One of the minimum demands consisted of reparations for damage caused to the Soviet Union by Rumania in the period of hostilities and occupation. At issue was the establishment of an obligation: there was no mention at this stage of the amount and composition of deliveries to be made. Britain and the United States approved the Soviet proposal with small changes mainly concerning future frontier arrangements.³³ The State Department had already noted earlier in the year that in principle Rumania owed compensation to the United Nations.³⁴

In the terms proposed to Rumania it is noticeable that the amount of reparations is not mentioned in detail whereas in Finland's case the precise sum was known early in April. This omission was evidently because the Soviet Union first announced the reparations term in principle — as in the case of Finland earlier. If the negotiations had reached the detailed stage the sum would probably have been specified. Only when the original figures are published will it be possible to say whether the sum

32) MacWeagh from Cairo to SD 8.4.1944, FRUS 1944 IV, pp. 169—170.

33) Lundestad 1978, pp. 223—225 and sources mentioned.

34) SD to Winant in London 2.2.1944, FRUS 1944 IV, p. 140.

was 600 million dollars.

However, Britain and the Soviet Union were in some disagreement over reparations. In London the reparations article for Rumania was considered auspicious because it remained on the level of general principle. The British interpreted this as meaning that the Kremlin now assented in the case of Rumania to the reservations which London had about naming the actual reparations sum. On the other hand the British had agreed — with qualification — to a reparations demand based on a specific sum for Finland. Before the break in negotiations the Soviet Union had given no sign of willingness to specify the reparations sum for Rumania too. Thus the attitudes of Britain and the Soviet Union were not yet fully clarified.

In April the German hold on Rumania was powerful, and Rumania's mistrust of Soviet aims was evident. No armistice was achieved at this stage, but a new possibility arose when Rumania's Ambassador in Stockholm, Nanu, received easier terms from the Soviet. The Rumanian government was guaranteed a free administrative area which foreign troops would not enter and was allowed a 15-day interval between a cease-fire and a declaration of war on Germany. A reduction of reparations was also promised,³⁵ but even these concessions did not settle matters. Instead, the Red Army advanced further into Rumanian territory, at the end of August came a change of regime in Rumania, and with it a change of sides in the war. On 22nd August a new government led by General Sanatescu announced that its first actions in foreign policy would be aimed at an armistice.

On 26th August Molotov informed Clark Kerr and Harriman that the Soviet Union was still prepared to make the three aforementioned concessions to strengthen the position of the new government.³⁶ With regard to reparations London could not understand these concessions because, in the British opinion, their sum had been left open, to be determined only at the peace conference. It was difficult to imagine a reduction of a sum which had not even been fixed.³⁷ Yet the Kremlin assumed that Britain

35) Lord Moyne from Cairo to FO 8.7.1944, FO371 44003 R10668/294/37 PRO.

36) Clark Kerr from Moscow to FO 26.8.1944, FO371 44005 R13271/294/37 PRO.

37) FO Minute (Reed) 26.8.1944 and FO to Clark Kerr in Moscow 26.8.1944, FO371 44005 R13271/294/37 PRO.

had agreed in April to the inclusion of a reparations article in armistice terms for Rumania. On 28th August Molotov announced that there was no further reason to leave the fixing of a reparations sum until the peace conference.³⁸

It was time, according to the Soviet concept, to move from the level of general principles to that of details, but Molotov still gave no hint of the actual sum. This was revealed to the British only on 31st August, when they received a complete draft of an armistice agreement.³⁹ Under its terms Rumania declared war immediately on Germany and Hungary, and the Allies occupied all areas of Rumania. Thus the Soviet Union finally "forgot" its earlier concessions.

The Soviet proposal was based on deliveries of Rumanian goods to the value of 300 million dollars in six years. The Americans very soon approved the Soviet principles. Though the State Department would have preferred to leave the sum unspecified, the Americans agreed to these terms when Molotov stressed the special importance which the Soviet Union attached to the matter. In Washington it was not believed that the Soviet attitude would change voluntarily. But the reparations question was not considered a sufficient reason for endangering Allied collaboration. The State Department urged Harriman, however, to explain to the Soviet government that as a matter of principle the United States wished to avoid mention of a specific sum until agreement was reached on an Allied reparations policy towards all enemy countries.⁴⁰

London, however, was not willing to agree to a named sum for reparations. Clark Kerr was sent a draft of a new reparations article in which the sum was not mentioned.⁴¹ Molotov did not agree, but demanded that 300 million dollars be mentioned. Clark Kerr informed the Foreign Office on 4th September that he did not believe he could change Molotov's attitude. In the Kremlin, stated Molotov, this article in particular was considered the most

38) Molotov to Clark Kerr 28.8.1944 and Clark Kerr from Moscow to FO 28.8.1944, FO 371 44006 R13472/294/37 PRO.

39) Harriman from Moscow to SD 31.8.1944, FRUS 1944 IV, pp. 205—206; SD to Leahy 2.9.1944, FRUS 1944 IV, pp. 208—212.

40) SD to Harriman in Moscow 5.9.1944, FRUS 1944 IV, pp. 221—223.

41) FO to Clark Kerr in Moscow 3.9.1944, FO371 44006 R13697/294/37 PRO.

important in the armistice agreement. Molotov asked again and again whether the British thought the sum in question too large. In Clark Kerr's opinion Molotov obviously did not believe that the British were pursuing a matter of principle — London's more likely purpose, he thought, was a revision of the sum concerned.⁴²

On no account did the Foreign Office wish to argue with the Soviets on the question of whether Rumania was able to pay reparations of 300 million dollars in six years. It was essential to remember the experience of German reparations after the previous war. Available data indicated, in the Foreign Office view, that the demand exceeded Rumanian productive capacity, so that the experience of Germany might be repeated. Also Rumania would set a precedent in the setting of reparation levels. Before a sum was fixed the Allies were obliged to agree on what damage, loss and expenses should be included in determining reparations for each country.⁴³

When Clark Kerr reaffirmed that His Majesty's Government could not agree to mention the sum which had been named, Molotov made "a short speech" on the extensive destruction suffered by the Soviet Union. The reparations article, he said, was at the heart of any armistice, without it an agreement would be worthless and could not be signed. In the spring His Majesty's Government had agreed to a named sum of reparations in the case of Finland, so that now he would evidently be obliged to inform his government and people that Britain had changed her attitude. At this stage Clark Kerr used his powers, producing a new draft article which went some way towards meeting Soviet demands, but Molotov was still not satisfied. He wished to be assured that the sum mentioned in the draft signified the Soviet share only, and proposed an addition for reparations payable to the other Allies. Clark Kerr again informed London that he did not believe Molotov would deviate from the original Soviet proposal. Clearly disappointed, Clark Kerr noted that he had received no support from Harriman, who had announced at an early stage that he would be satisfied with a settlement reached by Britain and the

42) Clark Kerr from Moscow to FO 4.9.1944, FO371 44007 R13955/294/37 PRO.

43) FO to Clark Kerr in Moscow 5.9.1944, FO371 44007 R13955/294/37 PRO.

Soviet Union.⁴⁴

The Foreign Office explained to Clark Kerr that Molotov's assertion of a British change of attitude was quite wrong. In the case of Finland the Soviet proposal had been agreed to primarily because there had been no time for discussion of the terms before they were communicated to the Finns. And there was no need to protest later, as the negotiations came to nothing. But in the Rumanian case Britain had consistently refused to approve the sum named, in addition to which the Soviet Union itself had approved a reparations article in accordance with British wishes regarding Italy.⁴⁵

Draft for an Armistice Agreement with Finland

Before the British and Soviet negotiations had time for a final discussion of the proposed agreement with Rumania, Molotov on 6th September presented the draft of an agreement with Finland. Only the Petsamo question emerged as a substantial subject of dispute between the Soviet Union and Britain. Harriman followed the arrangement of Finland's affairs as an observer only. In the original proposal Moscow required the Finns to pay compensation to the Mond Nickel Company, but London could not approve this since it was possible that Finland with her burden of reparations would be unable to pay the Anglo-Canadian company. In the second place it was unjust for the party relinquishing the territory to pay compensation. The area with its rights and obligations would be transferred to the Soviet Union, as any other solution would be difficult to explain to public opinion. The section dealing with compensation for Petsamo was removed from the draft and a compromise reached, the nickel company receiving 20 million dollars in compensation from the Soviet Union, who announced that it would take this sum from what was received from Finland.⁴⁶

On going through the terms intended for Finland with Clark Kerr

44) Clark Kerr from Moscow to FO 6.9.1944, FO371 44007 R14078/294/37 PRO.

45) FO to Clark Kerr in Moscow 7.9.1944, FO371 44007 R14078/294/37 PRO.

46) Polvinen 1980, pp. 106—117.

and Harriman, Molotov devoted great attention to the compensation paragraph. The Soviet demand had fallen from 600 million to 300 million dollars and the time for payment was extended from five to six years. Molotov made it clear that the reduction had been made in order to meet the British government's wishes. He supposed that the sum proposed could be approved in London.⁴⁷ Clark Kerr committed himself to nothing at this stage, however.

The reason given by Molotov was understandable, bearing in mind that Churchill had declared his opposition to large reparations at an early stage. During the spring and summer of 1944 the British had repeatedly expressed this attitude. From another point of view it was important for the Soviet Union to agree quickly on terms with its Allies so that countries which had fought beside Germany might soon be removed from the war. It was not worth weakening Allied collaboration for the sake of long negotiations on the substance of a single article. And to make an agreement at this stage would have the advantage of securing some results at least for the Soviet Union. When the major war ended the Western Allies might be unwilling to make an agreement, especially on reparations.

The Soviet Union had proposed earlier that half the damage caused should be made good. When the claim was reduced, that principle was relinquished. In March 1944 Molotov estimated the damage caused by Finland at 1,200 million dollars, but since the time concerned the sum had undoubtedly risen. Thus a claim for 300 million dollars would not have covered as much as a quarter of the total damage. In the terms for Rumania the Soviet Union intimated that 300 million dollars was a fifth of the total damage. For purposes of calculation on the above basis the sum for Finland too was a fifth of total damage, but in that case the damage caused by Rumania and Finland would have needed to be of the same degree. Because source material remains unavailable for the moment the basis of calculation cannot be made clear, but no sum representing the damage can possibly be more than an estimate. As the reparations sum for Rumania and Finland was the same and its proportion of the total damage was not to be mentioned in the final

47) Clark Kerr from Moscow to FO 6.9.1944. FO371 43164 N5405/30/56 PRO.

agreement, the sum was evidently arrived at on the basis of other factors. It is possible that without a precise basis of calculation 300 million dollars seemed a suitable liability on which the Allies reached an understanding.

Agreements for Rumania and Finland

In accordance with instructions received from London Clark Kerr on 8th September presented a new draft of the compensation article for Rumania. The reference to 300 million dollars as a proportion of the total damage (equivalent to a fifth) had been removed, and Molotov now agreed. A second change was that the British wished the word "provisionally" to appear before the sum in question. In practice this would have delayed the fixing of the final reparations sum until later, to which the Soviet Union could not agree. Clark Kerr was prepared to leave the word out if the Allies would sign a separate document stating that the reparations sum of 300 million dollars could be reconsidered if it proved too large for Rumania. A second article would mention that although the Soviet Union would receive 300 million dollars, the other members of the United Nations would also receive a sum



Sir Archibald Clark Kerr, Britain's Ambassador to Moscow. This career diplomat was one of the outstanding men in the British Foreign Service.

equivalent to a share of reparations from all enemy countries in the final agreement. Clark Kerr let it be understood that according to British calculations Rumania would be unable to pay the proposed reparations sum. Molotov stated, however, that the Soviet Union would not agree to sign such a document. British and Soviet views were in conflict, and Clark Kerr was obliged once more to ask instructions from London.⁴⁸

Negotiations between Britain and the Soviet Union on the subject of a reparations article for Rumania had reached a dead end from which London tried to find a way out. At the Foreign Office it was thought dangerous to let a Rumanian armistice collapse over this question, because on all other problems a solution had been reached. The Soviet could sign its own armistice agreement with the Rumanians, which would leave the British to make their own arrangements. Allied collaboration would have suffered as a result of this. The British also admitted that the Soviet Union had the primary influence in matters affecting Rumania. The Foreign Office doubted whether Rumania had any practical importance as a precedent. The problems of Germany were of a quite different order, however.⁴⁹ In the opinion of the Treasury, however, Rumania would set a precedent in any economic decisions bearing on Germany, and accordingly the Treasury held closely to the original British attitude.⁵⁰

Chiefly in order to maintain Allied collaboration the Foreign Office assented and on 10th September gave Clark Kerr authority to approve the Soviet reparations article. The Foreign Office stipulated, however, that reference be made in writing to the views of His Majesty's Government on two points. First, in the final disposition of reparations each creditor country should receive an agreed share of the reparations to be taken from all enemy countries. In London the settlement of reparations was seen as a whole — regardless of whether separate armistice agreements had been made, in the final peace conference reparations should be further deliberated, and if necessary the articles of agreements already made should be altered.

48) Harriman from Moscow to SD 8.9.1944, FRUS 1944 IV, pp. 226—227.

49) FO Minute (Howard) 9.9.1944, FO371 44007 R14185/294/37 PRO.

50) Treasury (=T) to FO 9.9.1944, FO371 44007 R14185/294/37 PRO.

Second, whatever happened in the case of Rumania, it did not mean that His Majesty's Government consented to that case becoming a precedent in other cases. In the Rumanian case, as in the others, Britain reserved the specific right to inquire into the observance of the article if British interests were endangered by full-scale reparations.⁵¹ These matters were contained in a letter from Clark Kerr to Molotov dealing with both Rumania and Finland and bearing the same date as the armistice agreements with these countries.⁵²

The Allies reached an understanding on the wording of the armistice agreement for Rumania as late as 10th September. The Rumanians tried in vain to obtain changes in the reparations article, and the agreement was signed on 12th September 1944.

Regarding the reparations article for Finland the Foreign Office waited for the decision on Rumania. Clark Kerr informed London that in April Britain had not been in favour of suggesting a particular reparations sum, nor was there a basis for fixing one in September. At issue was a struggle which the British were eventually to lose. To save time and avoid bitterness Clark Kerr recommended British assent to the terms in question.⁵³ As the Rumanian armistice was signed and the economic effects of the Finnish armistice terms could not be considered unduly heavy, London no longer had reason to reject the Soviet terms in this regard.⁵⁴

During the negotiations in Moscow the Finns did not obtain the relief they had proposed from their reparations liability. Foreign Minister Carl Enckell emphasized, quoting calculations by Finnish experts, that the reparations sum proposed was impossible for Finland to pay. He also inquired whether part of the reparations might be paid in dollars, in which case Finland could borrow the sum concerned. Molotov did not even engage in serious discussion of the matter. He contented himself with saying that he would read the Finnish memorandum only if the experts could prove that one year of war was cheaper for Finland than one year of peace with

51) FO to Clark Kerr in Moscow 10.9.1944, FO371 44007 R14185/294/37 PRO.

52) FO to Clark Kerr in Moscow 10.9. and 11.9.1944, FO371 44007 R14271/294/37 PRO.

53) Clark Kerr from Moscow to FO 9.9.1944, FO371 43164 N5476/30/56 PRO.

54) FO to Moscow Embassy 10.9.1944, FO371 43164 N5476/30/56 PRO.

reparation payments.⁵⁵

The reparations article had been agreed between the Allies, and the Soviet Union did not wish its formulation to be dependent on enemy attitudes. Enckell's proposal of money payments with loans was against the combined views of the Allies, who would therefore probably have rejected the Finnish proposal unanimously, above all the aforementioned parts of it.

The American and British desire to delay the fixing of a reparations sum until the peace conference may be regarded — as *Geir Lundestad* has shown in the case of Rumania⁵⁶ — as an attempt to limit Soviet influence in Rumania and Finland. Though the attitude of the Western Allies possibly had some such effect, this was obviously not the central motive.

The American and British wished to be careful, of course: they had no desire for the Soviet Union to benefit from large reparations. But if the intention had actually been to use reparations as an instrument of power politics, the Americans in particular would hardly have avoided disagreement and assented to the Soviet proposal as easily as in fact happened. The approaching Presidential elections, to be sure, may have contributed to the caution of Roosevelt's policy on these matters.

Reluctance on the part of Britain and the United States alike to approve a specific reparations sum and their attempt at least to leave the door open for a possible change, were due mainly to the fact that Rumania and Finland were setting a precedent in the settlement of the reparations issue. Reparations would have a powerful influence on postwar economic relations between states, and the Americans and British wished to play their part in bringing about a comprehensive settlement. It was to be feared that the Soviet Union would by its present tactics bring into effect a decision unsuited to such a settlement in connection with a peace treaty. There was a further danger that later the Kremlin would demand — especially for Germany — that the same principles be applied, appealing to the fact that the Americans and British had already agreed to them. In order to maintain collaboration,

55) Records of Finnish Armistice Negotiations, FO371 431 43179 N8137/30/56 PRO.

56) Lundestad 1978, pp. 226—227.

however, the Western Allies acceded to the vigorous Soviet demands.

British Needs

Britain's interest in Rumanian, Finnish and Hungarian reparations was due above all to important British commercial interests in Finland. In 1937 Finland took 14th place among the countries from where Britain imported and 21st among the countries receiving her exports. With Rumania and Hungary, on the other hand, trade was slight before the war and there would be few chances of improvement after it.⁵⁷ Now that the reparations of Rumania, Finland and Hungary were interlinked, the British were obliged to watch their interests in all these countries.⁵⁸

Table 1. British trade with various countries in 1938, 1946 and 1955 (mill. US dollars)

	Export			Import		
	1938	1948	1955	1938	1948	1955
Total	2602.8	6635.4	8467.6	4496.3	8374.5	10886.5
Rumania	6.8	3.9	8.4	18.7	13.2	9.8
Finland	28.6	81.7	121.2	94.2	140.4	210.7
Hungary	3.2	10.2	8.5	11.9	24.5	6.5

Source: Direction of International Trade 1958, pp. 115—117.

In the British Treasury's opinion Finland could not possibly pay reparations worth 600 million dollars to the Soviet Union even if she supplied nothing to Britain.⁵⁹ Thus by London's reckoning the Soviet demand was too big from the standpoint of both the British and the Finnish economies.

Although British interests in Finland were evident, they were

57) Cole 1956, pp. 187—188.

58) Hurstfield 1953, p. 473.

59) T Minutes (Keynes) 6.4.1944 and (Playfair) 6.4.1944, T236:91 PRO.

only a part of Britain's foreign economic relations. At the beginning of May 1944 the Ministry of Supply completed an estimate of the likely timber situation in the first year following the armistice.⁶⁰ This allowed for an armistice with Germany near the end of 1944, so that the estimate actually referred to 1945. Calculated for that year were both the requirement and the supply of timber at home and abroad. For pit-props especially, large imports from Finland were planned: the Soviet Union and the Baltic States would supply 225,000 standards and Finland 200,000, while from Canada the figure would be only 100,000 standards and from Sweden 50,000. An important role was thus reserved for Finland in the revival of Britain's mining industry after the war.

40 % of the pit-props imported by Britain in 1938 were bought from Finland. Such a high figure was not to be reached immediately following the war, for in 1945 Finland's relative share of pit-prop imports was only 29 %: but growth was rapid and the pre-war level was reached by 1947.⁶¹

Understandably, housing construction played a central part in the use of softwood in postwar conditions. Housing needs involved not only replacing dwellings which had been damaged or totally destroyed in the war. There was also pre-war inheritance of unsuitable housing as well as an actual shortage. The number of families had risen greatly during the war, while construction at the same time had satisfied only a fraction of the increased demand. It was reckoned after the war that about 1,700,000 dwellings were needed.⁶²

Housing took up 42 % of softwood supplies in 1946, and 30 % was still needed in 1948. As British exports revived sawngoods were needed more than before for packing export commodities, added to which was their use in industry and shipbuilding. Finland's share of softwood imports in 1938 was 23 %, while in post-war years it stayed well below this level.⁶³

60) *Timber. Estimate of Position in the First Year after an Armistice* Supp. Minute 2.5.1944, FO371 40912 U4519/4519/71 PRO.

61) Holopainen 1952, pp. 16—17.

62) Holopainen 1953, p. 26.

63) Ervasti 1955, pp. 196—197.

Although the Finnish share of British imports did not immediately reach pre-war figures, the British had full reason to expect important timber deliveries from Finland. When the above-mentioned plan was drawn up it was impossible to know what form Finland's political status would finally take, nor were production conditions known to the British, but to secure commercial independence and to find an expedient solution to the reparations question were in the British interest. This was also the aim of plans presented by Foreign Secretary Eden to the War Cabinet at the beginning of August 1944.⁶⁴

But Soviet reparation demands did not necessarily mean that Britain would obtain no Finnish goods. London was considering an alternative: that the Soviet Union should supply the reparation goods she obtained from Finland in exchange for goods exported by Britain to the Soviet. They did not wish to raise this possibility with the Soviet Union, however, because trade directly with Finland was cheaper. Finland had taken out loans before the war which London wished to be repaid. If Finland did not obtain export revenue there would be no question of this. For this reason it must be stressed to the Soviet Union that in the coming armistice or peace agreement the Finnish government must be required to place its export at the disposal of the United Nations. But Britain's wish to have the loans repaid should not be taken as the reason for this idea. It should be urged, instead, that the United Nations needed the exports in question, which should not in any case be allowed to reach the enemy through neutral countries. One exception could be made at once to this principle, for Finnish exports to Sweden must certainly be allowed.⁶⁵

Timber for the British

The 19th article of the Finnish armistice agreement directed Finland to place at the disposal of the United Nations such requisites and products as these nations might demand for war purposes.

64) Nevakivi 1976, pp. 199—200; Polvinen 1980, pp. 92—94.

65) FO to Moscow Embassy 9.4.1944 Board of Trade copy, BT11/2241 PRO.

Britain's credits due from Finland at the beginning of March 1944 were over 3.6 million pounds, while Finland's corresponding credits due amounted to less than 1.6 million pounds.⁶⁶ If the armistice and peace terms were not too heavy a burden and Finland were allowed to return to normal economic life, London expected no particular problem with the credits due. Finland's trade relation with Britain had been favourable and her reputation was good as a payer of debts. There was no wish whatever to push claims at the expense of Finland's economic revival — access to Finnish markets must be secured by proceeding with courtesy in this matter.⁶⁷

Also, a stricter attitude was required by London with respect to Britain's credits that were due. The Board of Trade warned against estimating the importance of credits due to Finland on the basis of advantageous trade, as the situation after the war might be quite different.⁶⁸ In the opinion of Lord Keynes Britain must first secure her credits due in any case. An agreement must be made with Finland obliging the latter to use the whole of her export surplus to pay the loans in question before the money was used for purchases elsewhere.⁶⁹ Keynes' view, however, was not shared by the Treasury, where the opinion was held that it was necessary to wait for the final peace terms imposed by the Soviet Union on Finland. The primary objective at all events was to start trading, which the payment of credits due must not be allowed to frustrate. For the payment treaty which was planned terms had been envisaged requiring Finland to pay her pre-war debts before starting trade elsewhere in the sterling area.⁷⁰

An appendix to article 11 dealing with reparations in the Finnish armistice agreement required the parties concerned to negotiate on the classification of goods and the confirmation of delivery time. Not only did the Allied Control Commission arrive in Helsinki during October 1944 but also a Soviet delegation concerned with reparations and they launched negotiations with Finnish

66) *Finland — Property Claims* Note by Trading with the Enemy Department 2.3.1944, T23686 PRO.

67) T Minute (Playfair) 7.3.1944, T236/86 PRO.

68) BT to T 21.3.1944, T236/86 PRO.

69) T Minutes (Keynes) 21.3.1944 and 28.3.1944, T236/86 PRO.

70) T Minute (Playfair) 30.3.1944, T236/86 PRO.

representatives on detailed arrangements for reparation commodities.

On 21st October the Chairman of the Control Commission, Colonel-General Andrei Zdanov, met Francis Shepherd, who had been appointed Britain's political representative. From the first Shepherd stressed Britain's wish to obtain timber from Finland, though without sidetracking Soviet demands. Zdanov stated that the Soviet Union had no objection to the opening of contact between Britain and Finnish suppliers. Timber, pulp and paper would surely be enough for both parties.⁷¹

From the standpoint of reparations the armistice agreement left two important questions open. It was not made clear how the nominal sum of 300 million U.S. dollars should be divided in terms of deliveries of various goods. The agreement included a short list which began with Finland's traditional exports: timber, paper and pulp. Correspondingly, from Rumania and Hungary also their traditional exports were demanded. The Finns therefore expected deliveries to be based mainly on the above goods.

The agreement also made no mention of how the goods concerned should be priced.

As negotiations proceeded towards the end of October the Soviet Union began to stress the role that metal industry products should play in reparations deliveries, and the Finns were obliged to start planning what was quite a new industry. This change of emphasis occurred at a time when the Control Commission had arrived in Finland and was gathering preliminary information on the country's productive capacity. It is possible that these first figures altered earlier notions of that capacity, for the country's metal industry had grown substantially during the war. If its production index is put at 100 for 1938, the figure was 120 by 1944 and had grown to 200 by 1948. Timber, paper and other branches of industry, on the other hand, never attained their 1938 production volume during the war.⁷²

Finland enjoyed conditions more favourable to production than many other countries engaged in the war. Cessions of territory, resettlement of population, the war in Lapland and many other

71) Shepherd from Helsinki to FO 22.10.1944, FO 371 43196/5799/56 PRO.

72) Sahavirta 1958, pp. 39—46. Lehtinen 1967, p. 212.

burdens were of course heavy, but on the other hand the actual destruction caused by the war was confined to relatively limited areas. Fewer industrial installations had been destroyed than in central Europe, for instance. In Finland, unlike in Rumania and Hungary, there was no Allied army of occupation whose upkeep would have been a great expence.

As a timber-exporting country the Soviet Union understandably laid stress on the metal industry in its reparation demands. It followed from this that Finland was able to export her woodprocessing products elsewhere, chiefly to Britain. This undoubtedly made it easy for the British to accept the Soviet terms with regard to this item.⁷³

If Finland had been obliged to export her only vital export material free of charge, no foreign currency would have reached the country. She lacked many important industrial raw materials and machines, nor was reconstruction possible without substantial imports. Seen from this angle, the Soviet stress on capital goods was advantageous for Finland, as for others.

The Soviet demand for Finnish industrial products was not made, however, without raising problems for Britain and the United States. The Finns were not capable alone of meeting the reparation demands, but machinery and raw materials passed from the West through Finland to the Soviet Union. Thus the Soviet Union increased the quantity of metal industry products allocated to it following the end of the war. In the West it was reckoned that the Soviet Union was deliberately trying in this way to benefit at the Western Allies' expence.⁷⁴ This was certainly an important reason for the suspicion aroused by reparations, especially in the United States. *Daniel Yergin* has asserted that at a later stage the Soviets saw the Marshall Plan as an alternative form of reparations — but for them a less satisfactory one.⁷⁵

73) *Caplan: Preliminary Notes on the Principal Economic Consequences of the Armistice.* Shepherd from Helsinki to FO 22.11.1944, FO371 43200 N7730/5976/56 PRO.

74) Shepherd from Helsinki to FO 19.11.1944, FO371 43169 N7253/30/56 PRO.

75) *Yergin* 1978, p. 317.

Reparations and Economic Collaboration

At the end of November a stage was reached in Soviet-Finnish negotiations at which the Soviet Union announced — when the Finns tried to exert an influence on the composition of deliveries⁷⁶ — that all possible concessions had been made. Zdanov communicated this to the Finnish delegation led by Enckell on 29th November. The Foreign Minister tried to describe the situation to the members of his delegation by a gesture reminiscent of hanging. This did not go unnoticed by Zdanov, whose immediate reaction also revealed the Kremlin's aims. Zdanov was angrily surprised at the Foreign Minister's poor sense of reality. If the Soviet Union actually wished to do what Enckell had conveyed by his gesture, it need do no more than wait calmly while the workers returned to their factories which stood empty for lack of orders and raw materials — with the consequences which this implied. At that moment, Zdanov admitted, the situation for the metal industry was impossible, but it could be overcome by expanding the industry as the Soviet Union had done in its time. When reparation deliveries were completed the Soviet was prepared to give Finland a sufficient number of orders, so that expansion would be beneficial in the long term also.⁷⁷

What Zdanov's attitude shows above all is the Soviet wish to find through reparations a basis for long-term economic collaboration between the two countries. Although it was part of the Soviet purpose to demand — on the principles expressed during the war — the satisfaction it considered justified for the destruction it had suffered, reparations were, most importantly, a guarantee of co-operation in the future. Timber was not needed by the Soviet Union, and diversification of Finnish production was therefore the most practical solution at that time. It is undoubtedly an exaggeration to maintain that the reparations programme "saved" Finland economically, yet it is also certainly true that the decisions then made had lasting beneficial effects on Finland's economic development.

Later studies have shown that the reparations timetable and list

76) See e.g. Paasikivi 1985, (= Paasikivi's Diaries) 25.11. and 27.11.1944.

77) Harki 1971, pp. 48—49.

of goods were not in themselves a problem to the Finns. The worst problem in several industrial branches was to obtain domestic and foreign raw materials as well as machinery. *Jensen* comes to the conclusion that the burden of reparations as a whole — without belittling some indisputable difficulties — was not as heavy as generally supposed. By 1952, for instance, the metal industry had expanded considerably more than the reparations liability required,⁷⁸ which shows that this industry had a natural capacity for growth.

From that time until the present there has been some wish in Finland and in Western countries to interpret reparations as a screw tightened by the Soviet Union at Finland's expense. By forcing the Finns to build a new industry which after reparations would be dependent on Soviet markets, the Kremlin acquired an effective means of pressure. Thus, knowing their dependence, the Finns were compelled to follow a line friendly to the Soviet Union. According to this conception the "traditional and natural" focus of Finland's exports was only to be found in her woodprocessing industry directed to Western markets.⁷⁹

We must await the publication of original material to know whether Soviet political leaders entertained such thoughts when they put the main stress of reparations on metal industry products. However, that industry grew to have an important status in the country's economic life. Undoubtedly the metal industry with its direction towards Soviet markets can be looked at from the angle of dependence and pressure between buyer and seller. But it should also be asked whether Western countries have not at least as important a means of exerting pressure in relation to woodprocessing exports.

Britain and the Pricing of Reparation Goods

There was satisfaction in London when Moscow demanded reparations mainly in the form of metal industry products, so that

78) *Jensen* 1966, pp. 109—111.

79) See e.g. *Allen* 1960, p. 40; *Aubrey* 1961, pp. 227—228; *Junnila* 1964, p. 93; *Kovner* 1961, pp. 60—61.

timber remained available for export to Western markets. In the pricing of reparation goods, however, the British were disappointed. When negotiations started the Soviet delegation mentioned no particular price basis to the Finns, who therefore believed that world market prices at the time of delivery would be the basis for pricing reparation goods. On 18th October, however, the Soviets declared that some pre-war price level could be adopted. As the quantities proposed for delivery by the Soviet delegation grew in the course of negotiations the Finns expected a speedy settlement of this question. At the beginning of November the Soviet Union stated that in the course of peace feelers during March 1944 Molotov had mentioned, when speaking of the 600 million dollar reparations term, that deliveries should be made at normal prices. This had signified prices prevailing before the war or, to be more precise, prices in 1938, the last year of peace. According to the Finns Molotov had mentioned that goods would be priced at their "current" value.⁸⁰

Whatever had been said in Moscow at the time, the Finns found the Soviet demand unjust. For raw materials and machinery the Finns would have to pay prices which had risen during the war and would change during the period of reparations. It was also unjust that in the armistice agreement reparations of a given quantity should have been agreed but their actual value left dependent on future prices. In the Finnish view an interpretation which diverged from world market prices was against the spirit of the reparations article.

During the war commodity prices had risen so much that, reckoned at the 1938 price level, the Finns maintained that they would have to deliver some 600 million dollars' worth of goods. It was calculated later that in the reparations period lasting till 1952 — having obtained some relief from the original programme — Finland paid a total of 444.7 million dollars at the price level of the time of delivery and 546 million dollars at the 1952 rate.

The Finns believed that since spring 1944 the Soviet attitude to pricing had changed. Available material neither confirms nor contradicts this idea. With good reason the Soviets might say that in the situation of autumn 1944 there could be no talk of "normal"

80) Auer 1956, p. 17.

or "current" prices. After the war prices were expected to fall sharply. Another possibility is that in March the Soviet Union still had no firm notion of pricing. The list of reparation goods was decided only when the Control Commission came to the country and Finland's capacity for delivery was elucidated. It is possible that prices were fixed on principles which were settled in this connection.

The armistice agreement left open both the composition of reparations deliveries and their pricing. This may have happened not inadvertently but in order to make an appropriate reparations demand possible. The armistice agreement as such did not exactly define the actual composition of reparations, which were specified in yearly delivery programmes. The Soviet Union also agreed to changes in the original programme, so that Finland's reparations were conducted — so far the creditor was concerned at least — more flexibly than has been generally understood.

The Soviet demand for a 1938 price basis caused resentment not only in Finland but also among the Western powers and in Sweden. In London the reduction of the reparations demand from 600 to 300 million dollars was regarded as a British achievement, and now the Soviet Union was seen to be making good its concession. Mistrust of Soviet policy grew on London substantially.

As long as Soviet archives remain closed the aims of the Kremlin cannot be fully verified, but the Soviet attitude to the whole question of compensation points to a different conclusion. From the first the Soviet had demanded deliveries of goods, regarding them as the only practical possibility for its own economic system. In other words the Kremlin expected a certain volume of goods whose reception could be fitted into its own economic plans. If variable world market prices had been relied on for the pricing of these goods, the quantity of goods would have varied, creating difficulties in the receiver's plans for their use. In the autumn of 1944 world market prices were considered exceptionally high and a fall was expected, whereas the 1938 price level gave a firm basis for pricing.

Inquiries during the autumn of 1944 had convinced the British that substantial quantities of timber should be bought from Finland if others did not intervene. In mid-November the Foreign Office decided to raise the question of reparation pricing with the

Soviet Union. At the same time it was decided that Finland might purchase raw materials against payment, but Britain, already in difficulties over credits, could not issue loans to the Finns.⁸¹

No American Support

Before raising the matter in Moscow Britain wished to be assured of United States support. At London's request the State Department informed its Moscow embassy that Britain opposed the Soviet demands on pricing. In principle the State Department agreed with the British argument. The Americans were advised to stress in Moscow that the United States had from the first supposed the prices to be those current on world markets. No other interpretation was reasonable. Because the United States was not at war with Finland she did not wish to intervene in Finnish reparations. In the Rumanian case the United States had similarly resisted the pronouncement of a specific sum as compensation. The sum appointed for Rumania was high in relation to the country's payment capacity, and no interpretation which raised it could be approved. The Soviet Union's right to compensation for its losses must give way to the needs of European reconstruction and the United States' own interests.⁸²

In practice, however, the United States had no wish to act in the matter of reparations. The formal reason was that the United States had received no confirmation from the Soviet Union of the principles to be applied over pricing. During the war the Americans wished to avoid inter-Allied disputes on a question which was of secondary importance from Washington's standpoint. It was known that Molotov would adamantly oppose any change in the armistice agreements proposed, and the Soviet Union would not withdraw the interpretation it had already given. The British proposal had very little chance of approval. As the Hungarians were aware of the armistice terms for Rumania and Finland they might pay attention to the pricing question. To be bound to the British proposal in no way suited the United States'

81) FO Minute (Nutting) 14.11.1944, FO371 40999 UE2338/23/77 PRO.

82) SD to Kennan in Moscow 23.11.1944, FRUS 1944 IV, pp. 262—263.

purposes.⁸³

This American reasoning caused annoyance in London: the Soviets were known to dislike giving information voluntarily, but Washington could ascertain matters by asking its representatives in Bucharest. The Foreign Office finally acted without American support. The British believed the Finnish interpretation of the talks held with Molotov while understanding that there was no wish for such a view to be made known in Moscow. It was understandable — so London conceded — that the Soviet Union should protect itself against an exceptional price level. But to apply the world market prices current at the time would have been an equitable solution, because these prices, raised by inflation, also worked to the advantage of the Soviet Union in the form of increased export revenues — deliveries to Britain, for instance, were based on them. The motive for Britain's attitude — as the Soviet government was informed — was her own interest in the matter, because the more Finnish and Rumanian exports took the form of reparation deliveries, the less hope Britain had of obtaining the commodities she wished. But it was not in the Soviet interest to prevent such debtor countries from paying for imports without which reparations deliveries would be broken off.⁸⁴

To the Soviet Union the British spoke of a difference of interpretation — there was not even a hint of revoking the concession granted. It was a basic argument in London that if the armistice signatories — including therefore Britain — had wished to fix the prices of reparation goods at some past value, they would presumably have mentioned this in the terms. It was not part of the armistice agreement to apply local prices or exchange rates or a price level which had prevailed earlier. To observe world market prices would not only have protected the Soviet Union from unduly high local prices, but would also have secured the advantage of increasing deliveries if the expected fall in world market prices occurred.

The Finns did not learn of these British moves in Moscow. Instead, Finland's representatives tried in vain to convince the

83) Harriman from Moscow to SD 10.1.1945, RG59 740.00119EW1—1045 National Archives (=NA).

84) FO to Moscow Embassy 17.11.1944, FO371 40999 UE2338/23/77 PRO.

Soviets of a solution based on world market prices or — for instance — an average of 1936—1938 prices. On 25th November Zdanov stated that the value of reparations deliveries could be raised from the 1938 price level by 15 % for capital goods and by 10 % for consumer goods. Some forms of relief desired by the Finns were also granted in the composition of the reparations programme and in quantities of goods.⁸⁵ A few days later Shepherd hinted to the Finns that, on the one hand, the 1938 price level was hard for the Finns but, on the other, the 1944 level was impossible for the Soviets to approve; it would thus be worth while to pursue a compromise on the basis of delivery times — a solution the British had proposed in Moscow.⁸⁶

Shepherd learned that Zdanov had asked Finland for an answer by the 29th, when Britain's proposal in Moscow would have had no importance. In Helsinki the British tried to induce the Soviet Union to change its view, but the positions of the Allies remained far apart. In the Soviet opinion pricing was a matter between Finland and the Soviet Union in which Britain had no reason to intervene. They stressed two facts to the British in Helsinki. First, by lowering her standard of living Finland had every chance of discharging her reparations. Having avoided wartime destruction, the United States enjoyed an economic advantage which was clearly impressive, and the Soviet Union, by consistently reparations from Germany and all her allies, could reap advantages to its security and economy alike.

The second argument was also a principle of justice emerging from the war: it was for the attacker who had caused great material destruction and human suffering to make good his deeds. It was unjust that the Soviet Union should be in a worse position than the attacker at the end of the war. Without reparations Germany and her allies might rise from wartime destruction more quickly than the Soviet Union. With reference to Finland the Soviet Union stressed particularly the destruction and suffering caused in the Leningrad region.⁸⁷

Britain for her part had one aim only: to secure timber and pulp

85) Hyvämäki 1977, p. 252. Paasikivi's Diary 19.11. and 25.11.1944.

86) Shepherd from Helsinki to FO 27.11.1944, FO371 43170 N7913/30/56 PRO.

87) See also Krosby 1978, p. 45.

from Finland. At issue was no concern over a correct interpretation of the armistice agreement, pursuit of a consistent policy or sheer friendship for Finland. Reparations should simply be as small as possible, so as to allow Britain to obtain many commodities without needing to export raw materials to Finland.

Before the meeting of Soviet and Finnish representatives on 29th November Shepherd wrote to Zdanov⁸⁸ expressing London's dissatisfaction with the 1938 pricing basis and declaring that the matter had been raised in Moscow. These British views had no effect, however. A few days earlier Zdanov had talked to Prime Minister Paasikivi and assured him that the Soviet Union would not retreat from its attitude. Stalin had himself decided, and Rumania had accepted the decision on 25th November. The Finns must understand that this was not a business deal but a political levy. The Soviet Union had brought the war to an end and given Finland an opportunity to withdraw from it without occupation of the country. If agreements was reached on the pricing of reparations many other matters would be resolved easily.⁸⁹

British Left Aside

On 29th November the Finns announced their acceptance of the Soviet pricing proposal. On the same day the Soviet Union delivered a list of goods to be supplied by Finland as reparations. Final composition of the programme was so prolonged, however, that a basic agreement was not signed until 17th December 1944.

Despite this Finnish decision the British continued to defend their own attitude. In Helsinki the Soviet representatives did their best to avoid meeting Shepherd, who nevertheless made contact with Minister Pavel Orlov, political adviser to the Control Commission, on the last day of November. The latter regretted the way Britain had put pressure on her ally. A few days later Orlov revealed to Shepherd that the Soviet Union intended to apply the 1938 price level only until normal trade relations between the

88) Draft of Shepherd's letter to Zdanov (English and Russian) 29.11.1944, FO511:109 PRO.

89) Paasikivi's Diary 27.11.1944.

Soviet and Finland were restored, a period of one or two years in Orlov's estimation.⁹⁰

The thought of a temporary application of the 1938 price level emerged only in talks between Shepherd and Orlov. The Soviet Union did not officially confirm it later, nor did the British return to it. Despite this the talks show that the Soviets were at least considering a relaxation of their stand on the price question. The Finns had also proposed that the 1938 price level be applied until the figure of 300 million dollars was reached.⁹¹ It is especially notable in the opinion expressed by Orlov that application of the 1938 price level was linked to the return of normal trade relations and not for instance to a specific period such as two years. This indicates that the Soviet Union attached considerable importance to the reopening of trade with Finland.

While stressing the part to be played by metal industry products in reparations, the Soviet Union promised sufficient orders for these products on completion of the reparations programme. The Soviet also agreed to supply grain to Finland. Undoubtedly the arrangements announced by Orlov would not have been to the Soviet advantage. They would have shown that application of the 1938 price level had no logical connection with the armistice agreement.

Emphasis on the metal industry in the delivery programme suited Britain's designs well, but the pricing issue threatened British interests. For this reason London was not yet willing to give up the game, but expected the Kremlin to answer His Majesty's Government's letter. When there was no sign of an answer Embassy Counsellor John Balfour on 10th December sent a new letter to Molotov. This stated that the British government had not abandoned its attitude to the pricing question despite Rumania's and Finland's compliance with Soviet demands.⁹² The Foreign Office also expressed its wish that the Americans in Moscow be informed of the situation and their support obtained for the Rumanian solution. Bucharest and Helsinki were informed that discussions with the Soviet Union could not yet be considered

90) Shepherd from Helsinki to FO 3.12.1944, FO371 41000 UE2485/23/77 PRO.

91) Paasikivi's Diary 25.11.1944.

92) Balfour from Moscow to FO 10.12.1944, FO371 45744 UE467/20/77 PRO.

decisive, but talks on pricing would continue.⁹³

The Soviet answer was given only when the basic agreement had been signed, and the British were thus faced with a *fait accompli*. The attacker's duty to make good the destruction he had caused was restated in the answer, as was the fact that a fixed price level gave Rumania and Finland a basis for returning to normal economic conditions. An attempt was made to lessen British fears by insisting that the agreement would have no adverse effect on the Finnish and Rumanian economies. After deliveries had been made there would still be goods remaining for export, as timber and paper composed only a third of reparations.⁹⁴

Britain's resentment was not reduced by the Soviet answer, however. Shepherd had been completely ignored in the course of events, and London had no intention of accepting defeat easily. There was some thought at first that another solution might be attempted with the United States' support.⁹⁵ But in practice the game was played out, for the Americans had even less reason than before to bind themselves to the British proposal. There was no foundation for further action. The agreement which had been made would probably enable Finland's economy to be preserved and guarantee an export surplus for Britain. All that could be done was to bear in mind the promise made by Orlov to Shepherd that the 1938 price level would be applied only until normal trade relations were restored. With Hungary and Germany, on the other hand, the aim was to define the basis for the pricing of reparation goods in the agreement.⁹⁶

Armistice with Hungary

Allied negotiations on the armistice terms to be offered to Hungary were of current importance from mid-October 1944 onward, when agreements with Rumania and Finland were signed. The Soviet

93) FO to Moscow, Bucharest and Helsinki Embassies 9.12.1944, FO371 41000 UE2518/23/77 PRO.

94) Balfour from Moscow to FO 19.12.1944, FO371 41000 UE2734/23/77 PRO.

95) Shepherd from Helsinki to FO 19.12.1944, FO371 41000 UE2733/23/77 and FO Minute (Haigh) 21.12.1944 FO371 41000 UE2734/23/77 PRO.

96) FO Minute (Pink) 22.12.1944, FO371 41000 UE2734/23/77 PRO.

proposal was based on these agreements. In the 13th article the reparations sum was set at 400 million dollars (while for Rumania and Finland it was 300 million in six years) and the time allowed five years.

British and United States views on the weakness of the debtor's payment capacity, the necessity of international free trade and the bad experiences after the First World War were emphasized out more strongly than before with reference to Hungary. This was due in the first place to Allied political interest in Hungary. In October 1944 Prime Minister Churchill and Foreign Secretary Eden were visiting Moscow, where they wished — against the wishes of Roosevelt — to agree with Stalin on spheres of influence in eastern Europe. Although no actual agreement was signed, areas of relative importance were discussed. Churchill suggested for the Soviet Union a position of 90 % dominance in Rumania, and for Britain and the Americans together a similar measure of authority in Greece. In Bulgaria the Soviet Union would have 75 %, while in Hungary and Yugoslavia influence would be divided equally among the great powers.⁹⁷

Economic advantages were linked with political interest. In Hungary as in Rumania the Americans and British possessed an oil industry whose ownership became a matter of dispute between the Allies. It was also to be expected that reparations would be an encumbrance to the oil companies concerned. However, the Americans did not think it expedient to tell the Soviets that their wish to limit reparations was based on their own economic interests, although these in fact played a central role in the State Department's attitude.⁹⁸

During the Moscow discussions on spheres of influence Eden had an opportunity to tell Molotov that the Americans and British regarded 400 million dollars as too large a sum for reparations. The same day Stalin told Eden that he consented to a reduction to 300 million dollars, of which 100 million would be divided between Yugoslavia and Czechoslovakia.⁹⁹

97) Woodward 1962, pp. 310—312.

98) SD to Harriman in Moscow 14.10.1944, FRUS 1944 III, pp. 906—907; SD Memorandum (Luthringer) 21.10.1944, FRUS 1944 III, pp. 917—918. Lundestad 1978, pp. 229—230.

99) Kennan from Moscow to SD 20.10.1944, FRUS 1944 III, pp. 915—916.

The State Department was not satisfied with this proposal. In its opinion an appendix making matters more precise should be added to the reparations article, or the United States would reserve the right to raise the question of reparations again at a later stage. The United States wished the following of reparations deliveries to be in the hands of all three powers and outside the exclusive supervision of the Soviet Union; for this purpose a special reparations department should be set up in the Allied Control Commission. Only those goods directly connected with reconstruction, should be definable as reparation goods, which the receiving power should not then be able to export to a third country. Reparation goods obtained from current production must be priced on the basis of world market prices at the time of manufacture. The reparations timetable should also be so arranged as to disturb normal trade relations as little as possible.¹⁰⁰

An armistice with Hungary became possible at the end of December, when the Soviet Union presented a draft agreement.¹⁰¹ Regarding reparations the Soviet had taken note of the adjustments agreed with Eden: the sum was fixed at 300 million dollars and the time for payment at six years; of the total sum 100 million dollars were to be divided between Yugoslavia and Czechoslovakia. But the American proposal of a three-power reparations department and the British suggestion of a pricing system based on world market prices did not appear in the Soviet terms.

Molotov announced at the end of December that the American and British terms could not be approved. Reparations for Hungary should be regulated by the same principles as for Rumania and Finland — no economic or political factors had appeared to justify abandonment of the terms applied in those cases. The only matter to be considered was whether Yugoslavia and Czechoslovakia should be accepted as members of the Control Commission for the reception of reparations. Britain's representatives in Moscow felt that the Soviet Union might make one single concession under pressure: reduction of the reparations sum to, say, 240 million dollars.¹⁰²

100) SD to Kennan in Moscow 2.11.1944, FRUS 1944 III, pp. 922—925.

101) Harriman from Moscow to SD 27.12.1944, FRUS 1944 III, pp. 940—942.

102) Balfour from Moscow to FO 31.12.1944, FO371 48474 R83/82/21 PRO.

Americans Concede

In Harriman's opinion the reparations sum was not unreasonable. From the United States standpoint it might even be useful to tie the Soviet Union to the sum in question, because growth of appetite might have caused the Soviet to raise its demands. At the heart of the Soviet answer, in Harriman's view, was the wish to give the Americans and British no chance to take part in supervision of reparations deliveries: this would lessen their opportunities to oversee the economic life of Hungary and to direct the reconstruction of Europe. Harriman did not believe that the Soviet Union would easily change its attitude: he even proposed that the continuance of Lend Lease aid be made to depend on this.¹⁰³

Washington was unwilling to resort to such far-reaching measures but the State Department remained committed to the idea of a three-power reparations department. If this were not erected the United States would reserve the right to raise the question of compensation again if American economic interests were endangered. Compensation must also be guaranteed for the destruction of the property of the United States and the other Allies.¹⁰⁴

At the Foreign Office it was admitted that the Soviet Union could not be induced to give up the 1938 level in pricing or to agree to the formation of a reparations department. As, however, the Americans and British considered the agreements with Rumania and Finland opposed to the armistice conditions in principle, the British felt that they could no longer agree to a similar wording. In the cases of Rumania and Finland it could still be argued that the British had agreed in good faith to the proposed Soviet agreement, supposing as a matter of course that world market prices would be taken as a basis. This was no longer possible, and the matter must be clearly noted in the armistice conditions or an appendix. His Majesty's Government still took the view that no specific sum should be mentioned in the armistice agreement. If a sum were

103) Harriman from Moscow to SD 31.12.1944, FRUS 1944 III, pp. 951—953; for Lend Lease aid see Herring 1973.

104) SD to Harriman in Moscow 3.1.1945, FRUS 1944 III, pp. 954—955 and SD to Harriman in Moscow 6.1.1945, FRUS 1944 III, pp. 963—965.

mentioned, however, it must not influence a reassessment of the sum if the burden of reparations proved too heavy.¹⁰⁵

The State Department agreed in principle with the British view and did not directly refuse its support, but advised Harriman to follow primarily his instructions from Washington.¹⁰⁶

The Soviet Union held steadily to its view that a department to deal with reparations was not needed in the Control Commission. The Commission contained an economic department which would receive all information connected with reparation payments. After this promise the Americans were prepared to approve the article for Hungarian reparations. At the signing ceremony, however, the United States submitted a written statement reserving the right to raise the reparations question if need be. Before the delivery of this statement Molotov tried to show that it was unnecessary, as reparations could always be discussed through diplomatic channels. A separate statement merely weakened the armistice agreement. Harriman said he had received instructions on the matter which he was bound to follow. The statement was addressed only to Britain and the Soviet Union; it need not come to the knowledge of the Hungarians even if the United States were to consider its publication unavoidable. The Americans thus sought a means of exerting pressure on the Soviet Union to change its attitude. Molotov remarked curtly that the Soviet government might find it necessary to repay the Americans in their own coin. The discussion ended with Harriman remarking that the Soviet had every right to do so.¹⁰⁷

A Consolation Victory for the British

In Britain's view the Americans had again yielded too easily to the Soviet will, but this time London demanded that its own demands be taken into account. The Foreign Office gave its Ambassador in Moscow permission to inform Soviet representatives that Britain saw two alternatives in the prevailing situation. First, the armistice

105) FO to Washington Embassy 5.1.1945, FO371 48474 R83/82/21 PRO.

106) SD to Harriman in Moscow 9.1.1945, FRUS 1944 III, p. 967.

107) Harriman from Moscow to SD 9.1.1945, FRUS 1944 III, pp. 968—969.

agreement might contain an appendix stating that the pricing of reparations goods would be based specifically on the 1938 price level + 10/15 %. Second, the armistice agreement would be drawn up according to the Soviet proposal, whereupon Britain would hand a separate note to the Soviet government. In it His Majesty's Government would declare its opinion that world market prices were fair in this connection: it would not change this opinion even if the Soviet Union made an agreement on some other basis. In all probability the matter would then be made public.¹⁰⁸

Molotov did not yield at once to British pressure. The Soviet wanted an agreement similar to the terms it had given to Rumania and Finland even if Molotov promised, on the strength of Harriman's proposal, to inform the Hungarians in advance of the pricing basis. This was a mere formality, however, as the Hungarians were of course aware of the situation. This being so, in Harriman's opinion little would be achieved by the British proposal.¹⁰⁹

The British were annoyed by the Americans' unwillingness to perceive the principle underlying this matter. A change in the previous texts of the agreements and a specific mention of the pricing basis would show in factual terms that the procedure followed in the Rumanian and Finnish cases was not the right interpretation. The Soviets had misled the British over Rumania and Finland, and wished still to save their faces. Also the Soviet Union might lose its bargaining position in relation to the Rumanians and Finns if the altered text referring to Hungary should become public.¹¹⁰

On the evening of 15th January Molotov informed Balfour and Harriman that the Kremlin had agreed, besides some other concessions, to the proposal of His Majesty's Government to mention the 1938 price level + 10/15 % in an appendix to article 12 of the armistice agreement.¹¹¹ The British had won a consolation victory. To be sure, a certain sum was mentioned and pricing was still based on the 1938 level, but the mention of a pricing basis

108) FO to Moscow Embassy 11.1.1945, FO371 48474 R641/82/21 PRO.

109) Harriman from Moscow to SD 10.1.1945, FRUS 1944 III, pp. 969—970 and Harriman from Moscow to SD 14.1.1945, FRUS 1944 III, pp. 972—975.

110) Balfour from Moscow to FO 14.1.1945, FO371 48474 R1069/72/21 PRO.

111) Balfour from Moscow to FO 15.1.1945, FO371 48474 R1170/82/21 PRO.

added to the Hungarian agreement softened the defeats suffered by Britain in the regulation of the reparations question.¹¹² Once Britain, the Soviet Union and the United States had reached agreement on all terms of the armistice agreement, the Hungarian delegation from 18th to 20th January 1945 had a chance to state their own point of view. They tried to have the time for payment extended from six to ten years, but the Allies did not consent.¹¹³ The armistice agreement was signed on 20th January 1945.

Yugoslavia and Czechoslovakia were authorized to negotiate directly with Hungary so that Czechoslovakia should receive deliveries to the value of 30 million dollars and Yugoslavia 70 million.

Yalta: a Soviet Proposal

In the first year of reparations Rumania, Finland and Hungary began to deliver goods to the Soviet Union while German reparations again became the subject of Allied discussion. The Normandy landing of the Western Allies in June 1944 and the military action following it led the Allies into a situation where a decision had to be made out on the policy to be followed towards Germany. The position of Germany and thus the peace terms applicable to her — including reparations — differed from those of the above-mentioned countries. For instance, the Allies wished to ensure the dismantling and limitation of German war potential in future, so that definitive moves on reparations were in the foreground. But deliveries from current production — the chief basis for decisions already made — remained in the background because the construction of an industry for reparations might mean the growth of an industrial potential which would become dangerous. Thinking on these lines united the Allies. The views of Treasury Secretary Morgenthau were partly responsible for persuading the Americans.¹¹⁴

112) FO Minute (Sargent) 17.1.1945, FO371 48474 R1350/82/21 PRO.

113) Balfour from Moscow to FO 19.1.1945, FO371 48474 R1471/82/21 PRO.

114) SD Memorandum (Harriman) 20.1.1945, FRUS Malta and Yalta, pp. 176—178. Gaddis 1972, pp. 114—126.



V. M. Molotov, Soviet Commissar for Foreign Affairs.

The first combined Allied declaration on German reparations was made at the Yalta conference of 3—11.2.1945. At the second general session on 5th February the matter was raised by Stalin, who asked Maisky to introduce the Soviet proposal. This provided for a division of reparations into complete transfers of goods lasting two years and a delivery programme from current production lasting ten. Germany's heavy metal, electrical and chemical industries would be cut by 80 % and her armaments industry dismantled altogether. Germany was to be placed under strict three-power supervision, including a reparations commission to be set up at once in Moscow. Maisky also stated the principles on the division of reparations and demanded at least 10 billion dollars for the Soviet Union.¹¹⁵

All agreed that German reparations were such a complicated question that it could not be solved at a summit conference but should be left to the reparations commission to be set up in

115) Second Plenary Meeting 5.2.1945, FRUS Malta and Yalta, pp. 611—633.

Moscow.

Maisky's proposal showed that the Soviet Union still considered reparations a crucial question for Allied collaboration. The proposal centred on those principles which Varga had brought out in his article. Included was the mention of a reparations sum, which had led Britain and the Soviet Union into a dispute over the armistice agreements with Finland, Rumania and Hungary. This confrontation was repeated at Yalta in the discussion of German reparations.

Churchill and Eden strongly opposed the Soviet proposal. If German industry were dismantled so ruthlessly, poverty and even starvation would result. If this plan were carried out the Americans and British would have to provide for the Germans. For this reason a reparations sum should not be fixed and the time for payment should be shortened.

Roosevelt did not accept the Soviet proposal unreservedly. He wished to ensure that the Allies did not expect the Americans to pay reparations on Germany's behalf as they had done after the First World War. Nor would they agree to reparations which drove the Germans to starvation, for which the Americans might be blamed. "Our objective is seeing that Germany will not starve in helping the Soviet get all it can in manpower and factories and helping the British get all they can in exports to former German markets ... Leave Germany enough industry and work to keep her from starving."

The Finnish "Mouse-Trap"

The Americans had expressed similar reservations before. At the end of November 1944 in Stockholm a representative of the British Ministry of Supply had asked what the American attitude would be to the possibility of dollar credits for Finland. Referring mainly to experiences after the First World War the Americans had then announced their unwillingness to play the part of helper: dollars would not be given merely to allow the British to obtain timber, whereupon Finland would be able to buy raw materials and the Soviet Union would receive its reparations. This would reserve for the United States only the dubious right of helping Finland: "What right have the Finns or any others to suppose that it is the policy of

the United States to give money to the Finnish mouse-trap.”¹¹⁶

In answer to the inquiries about credit the State Department sent instructions to Herschel Johnson, American Ambassador in Stockholm, to the effect that it would be extremely unwise to adopt a policy of aid for countries paying heavy reparations. The United States did not wish to pay reparations for others, as after the First World War, but reparations should be fixed according to the payment capacity of the debtor. If the United States were to give economic aid, they would adopt a different method.¹¹⁷

Yalta: the U.S.S.R. and the U.S. reconciled

At Yalta Maisky insisted that the Soviet programme was not unreasonable. 10 billion dollars represented only 10 % of the U.S. budget for 1945 or six months of war costs for Britain.

The reparations plan expressed orally by Maisky was distributed in writing at a foreign ministers' conference on 7th February.¹¹⁸ By its provisions the Soviet would receive 10 billion dollars' worth of reparations, Britain and the United States eight billion together and other countries two billion in all. These countries "have borne the main burden of the war and have organized victory over the enemy."

At a later stage of discussion Maisky presented Soviet calculations in more detail. A total of 20 billion dollars had been arrived at because when the war began German national assets were estimated at 125 billion dollars and when it ended at 75 billion. For industrialized countries transferable assets averaged 30 % of national assets or in Germany's case 22—23 billion. The Soviet proposed that 10 billion of this be transferred and that an equal sum from current production also be transferred over a period of 10 years. With the assets which remained the German living standard would be adequate if lower than, for instance, that

116) Caplan from Helsinki to Supp 5.12.1944 FO copy, FO371 43200 N7977/5676/56 PRO.

117) SD to Johnson in Stockholm 19.12.1944, FRUS 1945 IV, pp. 633—635.

118) Soviet Proposal on Reparations from Germany and Soviet Proposal on the Establishment of an Allied Reparation Commission (s.d.), FRUS Malta and Yalta, pp. 707—708.

in the Soviet Union. The reparations from current production would reduce the German national income by an estimated 5—6 %, which again was a reasonable demand.

The Soviet calculated reparations for Germany on a quite different basis from that applied to Rumania, Finland and Hungary. The principle of showing the total destruction caused by these countries and demanding a certain proportion of it as reparations did not serve in the case of Germany. In various connections the Soviet stressed the extent of the destruction caused by Germany — it was literally impossible to estimate — and the proportion of it which could be made good by reparations would be conspicuously small compared with the liability of Rumania, Finland and Hungary.

If the Soviet Union with the other Allies aimed at supervising and limiting German economic growth it was expedient to base calculations on the figures of German industrial life. That would lead in a direction which the Americans could accept: discussion of how much the debtor was able to pay.

Time was reserved for study of the Soviet proposal, and the foreign ministers began dealing with it on 9th February. In a counterproposal by the U.S. Stettinius suggested various changes of phrasing. In substance the important change was that in the American proposal the amount of the reparations would be the first object of study for the Moscow Reparations Commission, which should in this connection take note of the Soviet suggestion of 20 billion dollars.

Maisky demanded this sum "as a basis" for the work of the commission. After a moment's discussion Stettinius agreed that the commission should consider as a starting-point for discussion the sum of 20 billion dollars mentioned by the Soviet Union, which would receive 50 % itself. Once more the Soviet Union and the United States had easily reached an understanding and the British remained alone in opposition.

With the Rumanian, Finnish and Hungarian examples in mind Stettinius questioned Molotov on the pricing of reparations goods. Molotov confirmed that 1938 prices + 10/15 % would be followed as in the above-mentioned cases.¹¹⁹

119) Matthews to Stettinius 9.2.1945, FRUS Malta and Yalta, p. 816.

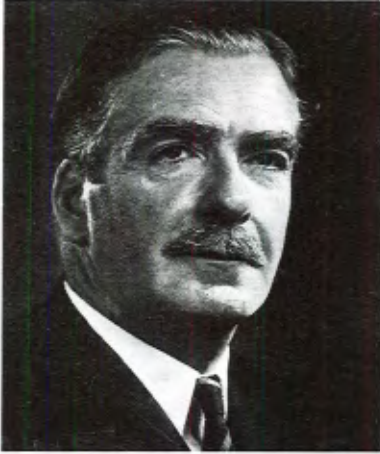
During the conference Maisky and Molotov tried in vain to persuade Britain to back the Soviet proposal. At a conference of foreign ministers on 10th February Eden submitted a British proposal in which a reparations sum was not mentioned at all. Suggested instead was the use of German manpower as a third form of reparations in addition to complete deliveries and current production. The British proposal showed that London did not oppose reparations on principle as long as they did not lead to an intolerable situation for the occupying power.¹²⁰

Maisky found Eden's answer very "disappointing". Without a specific figure of reparations the commission would have no basis or guideline for its work. Britain's attitude, thought Maisky, was inspired by the thought of taking as little as possible from Germany, and this suspicion was certainly increased by Eden's wish to shorten the period of current deliveries to five years. Stettinius in turn remarked that this period was only taken as a basis for discussion, nor was the Soviet Union bound to its demand of 20 billion.¹²¹

At a general session on 10th February Stalin tried once more to obtain the agreement of his allies. In the agreements with Rumania, Finland and Hungary a reparations sum had been mentioned, and no special problems had arisen in these countries as a result — as the British had feared, the settlements reached then had become precedents. Stalin insisted that the Germans could pay what the Soviet Union asked and still live as well as their eastern neighbours. Maisky had given extensive statistical data which supported Stalin's estimate. Stalin suspected that the British still wished to leave Germany strong; if Britain did not wish the Soviet Union to receive reparations it would be best for her to say so directly. He went on to suggest that the conference should follow the American-Soviet proposal and allow the Moscow commission to take a reparations demand of 20 billion dollars as a starting-point for its work. A little later Stalin said — thus showing his willingness to negotiate — that the Soviet Union was prepared to

120) British Proposal on Reparations 10.2.1945, FRUS Malta and Yalta, p. 885. Clemens 1970, pp. 167—168.

121) Meeting of the Foreign Ministers 10.2.1945, FRUS Malta and Yalta, pp. 871—877.



Sir Anthony Eden, Britain's Foreign Secretary, who opposed the American-Soviet proposal on German reparations.

take the sum in question as a basis for discussion. The Moscow commission could either raise or lower it: "we shall bring our figures to the commission and you will bring yours."¹²²

Stalin named this draft submitted by the Soviet Union an American-Soviet proposal. This hit the mark in that Stettinius quickly approved it. Later, to be sure, Roosevelt also associated himself with the British when the latter strongly criticised the Soviet suggestion, which some subsequent American studies have willingly taken as a sign that the United States had its reservations. But the actual settlement was reached at this stage by the foreign ministers, and other grounds can be found for Roosevelt's statement. A declaration of reserve concerning reparations was needed above all when he returned to the United States. In the second place the British could not be left quite alone: Roosevelt wished to be the mediator in this dispute between Britain and the Soviet Union.

According to the communiqué of the Yalta conference¹²³ Germany was obliged to pay reparations "in kind to the greatest extent possible." It was also stated that a commission had been set up in Moscow to consider how damage caused by the Germans

122) Seventh Plenary Meeting 10.2.1945, FRUS Malta and Yalta, pp. 897—911.

123) Communiqué issued at End of Conference 12.2.1945, FRUS Malta and Yalta, pp. 968—975.

should be made good.

In a secret protocol¹²⁴ it was stated that the three great powers agreed that Germany must pay primarily those countries "which have borne the main burden of the war, have suffered the heaviest losses and have organised victory over the enemy." Reparations were to be obtained within two years of the German surrender in the form of transfers of capital goods, deliveries from current production and use of German manpower. To put these principles into practice a Reparations Commission was set up in Moscow with representatives of all three countries.

The protocol continued by saying that the Soviet Union and the United States had agreed that the commission would take as a basis for discussion the Soviet government's proposal that the value of all-inclusive goods transfers and deliveries from current production should be 20 billion dollars, of which half should go to the Soviet Union. The British delegation was of the opinion that no sum should be mentioned.

At the Yalta conference agreement was reached on the principles of the occupation and supervision of Germany; these included unconditional surrender, division of Germany into zones of occupation, an invitation of France to join the control commission and to take charge of one zone, and the uprooting of Nazism from Germany. The principles of reparation were approved almost entirely in the form suggested by the Soviet Union. It was easy for all parties to accept the principle that reparations should take the form of goods deliveries to be divided in proportion to the burden borne and the destruction suffered.

Only in the matter of the reparations sum did Stalin fail to get all he wanted. To the last he tried to induce the British to agree to mention the sum: Stalin said he was afraid to tell the Soviet people on his return that they would receive no reparations because of British resistance. Churchill assured him of his wish that the Soviet would receive large reparations. All were agreed on a public announcement that Germany would be obliged to pay reparations "to the greatest extent possible." In the protocol of the conference, however, the British did not bind themselves to the "American-

124) Protocol on German, Reparation 11.2.1945, FRUS Malta and Yalta, pp. 982—983.

Soviet" mention of a 20 billion sum for reparations, but required the Moscow Commission to fix the sum.

Yalta: Agreement Within Reach

As earlier in the armistice agreements for Rumania, Finland and Hungary, Stalin at Yalta had succeeded in binding the United States to his reparations proposal. Mention of the sum — whose final amount could still have been discussed in Moscow — would have meant that the same concept was applied as for Rumania, Finland and Hungary. Without attaching any precise reasons to their demand the Soviets at Yalta presented a maximum programme which Germany in their opinion could carry out. The debtor would be assigned a reparations liability — which could be reduced after bargaining — up to a certain dollar sum, and the debtor himself would be responsible for its collection. Results were incomplete at Yalta because of British resistance: "Had circumstances been slightly different, the United States would have acceded to the Soviet request for ten billion dollars in reparations."¹²⁵

Foreign Office dissatisfaction was directed in particular at Stettinius, who had been quite incapable of opposing Soviet suggestions in negotiations between the foreign ministers. It was surmised in London that the United States wanted no reparations for itself, and therefore wished to involve itself as little as possible in the regulation of the matter.¹²⁶

Britain's opposition to the Soviet suggestion was primarily because the occupation zone proposed for the British was a heavily industrialized area. Removals of plant and machinery were to be expected mainly from this area, but no practical solution to the food supply problem was in sight. Germany and the duties of her occupiers had to be examined as one whole — a fact that the Americans were fond of stressing later.

The Americans for their part were willing to make a concession to the Soviet Union in one matter so as to gain advantages

125) Clemens 1970, pp. 168—170.

126) FO Minute (Coulson) 20.2.1945, FO371 45775 UE749/624/77 PRO.

elsewhere. From the United States viewpoint the Soviet proposal was not unreasonable but provided an easy occasion for letting the Soviet Union have its way. More troublesome was the British attitude, but while the war continued and anti-German feelings prevailed it was expedient for Roosevelt to incline toward a more severe reparations programme.

It should be stressed, however, that Soviet and British views at this stage were not very far from each other. In all other respects than the mention of a reparations sum the Foreign Office found the Soviet proposal well suited to British interests. Reparations from current production were a starting principle approved by Britain.¹²⁷

In the Soviet proposal all-inclusive transfers — not included at all for Rumania, Finland and Hungary — were placed before current production as a share of German reparations. An addition was the use of German manpower, which was linked later to the decision over prisoners of war. Stalin and Molotov explained that the Soviet intended to use two or three million Germans for reconstruction in the Soviet Union over a period of 10 years. They would be chosen initially from among those guilty of minor war crimes, and secondarily from among the unemployed.

127) *ibid.*

Reparations and the Occupation of Germany

Americans as Occupiers

Returning from the speeches of Yalta to everyday tasks Roosevelt experienced a disappointment: Stalin did not respond to his attitude with the concessions the President had hoped for. One source of disappointment was the formation of the Groza government in Rumania which Roosevelt considered an infringement of the Declaration on Liberated Europe agreed in Yalta. Dissension arose too over the ownership of the Rumanian oil industry and its role in reparations. Still more difficult was the political status of Poland: the London government in exile was regarded in Moscow as anti-Soviet, while the Lublin government was regarded in the West as a Soviet puppet.

In private talks during the last weeks of his life Roosevelt intimated that he was planning a "tougher" attitude to the Soviet Union. The granting of reconstruction credits was left to depend on whether the Soviet attitude changed, and the invention of an atomic weapon remained an American secret for the moment.

At the beginning of April after Roosevelt's death Harry S. Truman became President of the United States. As Vice-President he had been little concerned with questions of foreign policy. Truman wished to continue Roosevelt's line in essentials, aiming at an appearance of firmness in the hope of thus persuading the other party to collaborate and compromise. In the matter of reparations efforts were now made to achieve a settlement in which the Soviet Union with the other Allies would accept responsibility not only for supervision of the reparations

programme but also for its effect on economic life.¹²⁸

When spring came in 1945 Roosevelt had striven above all to ensure that he could not be accused at home of forcing American taxpayers to pay the debts of foreign states — including in this case a brutal enemy. The aim was to make the occupation as short as possible and thus to minimise its cost to the Americans. For this reason every effort should be made to ensure that Germany became self-sufficient, so that American credits and food deliveries were not needed to balance a trade deficit. This was the basis of the American demand that export revenues should be used primarily for the payment of essential imports, the so-called first charge principle. And because foodstuffs were more abundant in the Soviet occupation zone than in the Western zones, the American view was that they should be imported to the West, while other goods should be exported from the West in payment for these foodstuffs. For the achievement of balanced trade the whole of Germany should be treated as an economic unit.

The view of German reparations held by the Americans fitted into their total view of the German economy. Edwin W. Pauley, who led the United States delegation at the Moscow Reparations Commission, presented an equation which well illustrated the American attitude to this question. It was $R = P - (O + C + I)$, in which the amount of reparations from current production (R) was equal to production (P) less the sum of occupation costs (O), essential German consumption (C) and import (I).¹²⁹ The Americans emphasized that before reparations could be paid the German economy must produce an actual surplus. In practice this meant that reparations from current production could not have started for some time after the war ended. But the examples of Rumania, Finland and Hungary had shown the Soviet Union that despite post-war economic problems it was possible to carry out the reparation programmes as soon as the war ended, when the needs of creditors were at their greatest.

The so-called JSC 1067 instructions on the United States' German policy was aimed at the dismantling of Germany's

128) Gaddis 1972, pp. 120—124, 215—217. Paterson 1975, p. 239.

129) Pauley to Maisky 13.7.1945, FRUS Potsdam I, pp. 547—548. Paterson 1975, p. 251.

industrial potential and also at the establishment of a self-sufficient German economy. Moreover, the United States began to use its economic might to persuade the Soviet in favour of American plans for the creation of a post-war Europe. More openly than before the Americans used Lend Lease aid and possible credits for reconstruction as a means of political pressure.

In London, on the basis of the settlements with Rumania, Finland and Hungary, it was reckoned that the Soviet Union, strongly aware of the destruction it had suffered, had decided to obtain as many goods as possible from the enemy in order to raise its own living standard. The Soviet government wished to act in such a way, however, that its allies should intervene as little as possible in the handling of the Soviet share of reparations. The solution to the pricing question indicated that the Soviet Union wished to exclude all factors having a later effect on the volume of reparations. Britain's opinion was that the Soviet government had paid no attention at all to the payment capacity of the debtor: Soviet policy was to take as much as possible for as long as possible.¹³⁰

The progress of military action brought the occupation of Germany nearer day by day, but by the time Germany surrendered at the beginning of May the Reparations Commission established by the Yalta agreement had not yet started work in Moscow. The Soviet Union had been asked for the calculations underlying its reparation claim, but none had been produced. The British, for their part, were in no hurry to name their Moscow delegation. The United States and Soviet delegations were named in mid-March. Roosevelt had appointed Isador Lubin as leader of the United States delegation with Edwin W. Pauley as deputy, but Truman put Pauley, who was considered a harder negotiator in the leading position. Also included was an expert on the human relations side of reparations, which indicates that the Americans saw reparations not only as an economic question but also — and largely — as one of relations between occupiers and defeated.

Ivan Maisky was made leader of the Soviet delegation, and Sir Walter Monckton was finally appointed British representative.

130) *Reparation Obligations of Satellite Countries* FO Minute (Conrad) 14.4.1945, FO371 45776 UE1716/624/77 PRO.

The instructions received by Pauley¹³¹ took as the objective of the reparation plan — in accordance with the basic aim of American policy — the dismantling of German industrial potential. This was by no means in conflict with the need to develop trade and economic life in general — for Germany too — on a healthy basis. Thus neither the reparations settlement nor a rearmed aggressive Germany could endanger the primary objective — the creation of an "open door" policy. Also, the reparations plan must not necessitate construction of a reparations industry — which might leave Germany in a more favourable position than neighbouring states when reparations were completed, so that these states became dependent on Germany. For this reason reparations should be in the form of all-inclusive goods transfers as far as possible, but for political reasons it might be unavoidable to agree also to the principle of current production deliveries. Although reparations might lower the living standard of the Germans, they must not endanger their minimum livelihood.

In his memoirs Truman gives a picture of events which indicates already at this stage the American belief that little in the way of reparations could be obtained from Germany if it was intended to keep the country's economy active. Pauley's instructions contain no suggestion of the amount of the reparations, but undoubtedly the transfers of goods to be performed in the process of dismantling the war potential were expected to be considerable. The instructions presupposed no change in the principles of the Yalta agreement, but reparations were still seen as an important means of regulating Germany's post-war status. No American sources give the impression that Washington wished to limit reparations from Germany because of any substantial economic aid the Soviet might have gained from them.

At this juncture, according to Truman, the Americans were planning a method of collecting reparations based on the zones of occupation, although it emerged as an American solution only later — as eventually became clear. In the instructions to Pauley the zones are mentioned in only one connection: the reparations plan to be drawn up must result in an equal standard of living for

131) Instruction for the United States Representative on the Allied Commission on Reparations 18.5.1945, FRUS 1945 III, pp. 1222—1227.

each zone. It was of course desirable to avoid the spread of envy among the Germans because conditions were better under one occupying power than under another. This purpose was served also by the first charge principle: post-war food supplies must be assured on an equal basis for the whole of Germany area.

Monckton's instructions, in which Britain's policy was defined, demanded the satisfaction of minimum demands from the occupation forces and the Germans before payment of reparations. The task of the Control Commission was to determine which goods were indispensable for the livelihood of each occupation zone. German production was to be used primarily for payment of imports from abroad, and there were no grounds as yet for fixing the final sum of reparations. In accordance with their previous line the British wished the sum to be fixed at the peace conference, not before.¹³²

Summer 1945: a Change in United States Policy

When the war in Europe ended early in May the Allies acquired a new common concern. It was no longer a question of defeating the enemy: the occupying powers now had to consider the fate of Germany in peacetime. At the same time, however, the great powers seemed to be drifting more deeply into dispute. The San Francisco conference, intended to serve as an opening for the United Nations, threatened to become a forum for quarrelling rather than collaboration. When Germany surrendered the United States broke off Lend Lease deliveries to all countries except for materials needed in the war against Japan. Though this decision affected other countries besides the Soviet Union and Truman rescinded it later, the incident was bound to affect relations between the countries.

As the Moscow Reparations Commission at last began its negotiations the altered situation clearly influenced the attitudes

132) Reparations Memorandum by the Chancellor of the Exchequer C.P. (45)16 5.6.1945, FO371 45779 UE240/624/77 PRO. Cairncross 1986, pp. 80—86.

of those who took part. The United States began to dissociate itself from the Soviet idea of reparations. In concert with the British the Americans increased their efforts to persuade the Soviet Union to a united settlement which would also take note of Allied interests as occupying powers.

At the beginning of May, to be sure, George F. Kennan had advised from the American embassy in Moscow that it was no use expecting the Soviet Union to start serious negotiations. The Soviet government would make political rather than economic demands, and any attempt by the Western Allies to discuss economic matters would lead to mere "horse-trading".¹³³

The difficulties encountered by the occupying powers very soon taught the American authorities that goods deliveries were not, after all, an expedient form of reparation. But many Americans still saw Germany as a brutal enemy whose duty it was to make good at least part of the destruction caused. More and more frequently the American authorities prepared public opinion to understand that Germany would be incapable of paying substantial reparations. One such statement was by Pauley, published in the *New York Times* on 6th June.

One of Pauley's readers was General Lucius D. Clay, commander of the American occupation zone, who believed that considerable reparations could be obtained from Germany. He agreed with Pauley that German industrial production could not be set in motion for several years despite the fact that not more than 25—30 % of the country's industry had been destroyed. But Clay came to a different conclusion from Pauley: because the undestroyed industry was standing idle in any case and was thus outside the minimum needs of Germany, it could very well be removed as part of reparations.¹³⁴

In accordance with the Yalta decision Maisky in Moscow demanded that a German reparation sum of 20 billion dollars be taken as a basis for discussion. But U.S. policy had changed: on 19th June Pauley declared — without officially renouncing the Yalta decision — that there could be no discussion of a specific

133) Kennan from Moscow to SD 3.5.1945, FRUS 1945 III, pp. 1203—1205.

134) Clay to McCloy 29.6.1945, Papers of General Lucius D. Clay I, pp. 35—45. Paterson 1975, pp. 251—252.

sum of dollars before a preliminary estimate of Germany's payment capacity had been made. Also, before a total sum was fixed the demands of all countries entitled to reparations must be considered. Pauley and Monckton awaited the calculations on which the Soviet demand had been based.

The Soviet Union gave no statistics — data covering the whole country were hardly available at this stage, and statistics would hardly have resolved the disputes between the Allies. The work of the Reparations Commission was marking time because the Americans — to the satisfaction of the British — rejected the aim of finding a specific sum and thenceforth stressed the share of reparations to be received by each allied country. In the cases of Rumania, Finland and Hungary the Soviet Union had expressed a demand in dollars and subsequently supervised payment without Allied collaboration. The Americans and British did not want this situation to be repeated in Germany. If relative shares were fixed for the three great powers the Soviet would be forced to co-operate with the Americans and British in estimating the total sum of reparations and dividing it among the creditors. This had the advantage, in Pauley's view, of keeping the three great powers more closely together. This in turn would save the smaller allies from suspecting that their interests would be endangered.

From the division of reparations between the Allies it was a short step to the principle that each occupying power should receive reparations mainly from its own zone. The Americans certainly had in mind thus to place the Soviet in a situation where it must carefully consider whether large reparations could be demanded without the deliveries having a disastrous effect on the position of the occupying power. Zone-based reception meant little as a principle, as the Allies failed to make a joint decision and each occupying power had to be content in any case with reparations drawn from its own zone. This was in fact against the principle approved by the Americans, that Germany should be treated as an economic whole. It is true that Pauley tried to insist that there was no contradiction in this: reparations could be collected by zones and Germany still treated as one economic whole.

Pauley would personally have been prepared to change the U.S. reparations policy. He proposed that the Americans make their own demands — the only problem was, what goods could the Americans transport over the sea. Machinery and manpower were

not suitable in this connection, but suitable reparations for the Americans might consist, for instance, of gold, property abroad, patents and technical knowhow.¹³⁵

Washington did not believe that Pauley's plan was practicable, however. Pauley tried to insist that gold, for instance, would pay the expenses of occupation. The State Department did not change its view that it was not worth while for the Americans to procure large reparations — whether for a small economic benefit or for propaganda reasons. The main point was that all countries who had been under German occupation should receive a just share.¹³⁶

Pauley took advantage of a situation in which the Soviet Union either could not or would not present calculations of Germany's capacity to supply. If Germany were assigned reparations up to a certain sum of dollars without careful estimation of the country's industrial capacity, the demand in Pauley's opinion might fall short of what in fact was perfectly feasible. And the other extreme was also possible: the demand might become too large even if the German living standard were limited severely.

Preparing for Potsdam

The conference of the three great powers was approaching, but no conclusions had been reached in Moscow regarding the preparation for it. Pauley noted the questions which he thought should be answered before the Potsdam conference.

1. How were the three great powers to share among themselves the reparations considered to be available for this purpose?
2. How were the shares of the other creditor countries to be determined?
3. How were "reparations", "restitution" and "booty" to be defined?
4. Agreement to be reached on an immediate programme of provisional reparations for all creditor countries.
5. Principles for the management of reparations to be agreed upon.

On two of the above points an agreement was made on 12th July

135) Pauley to SD 19.6.1945, FRUS Potsdam I, pp. 510—511.

136) SD to Pauley 2.7.1945, FRUS Potsdam I, pp. 519—521.

allotting 56 % to the Soviet Union and 22 % each to the United States and Britain.¹³⁷

Negotiations centred on the question of whether to include France with the three great powers. Washington and London wanted to include her, but Moscow thought it unnecessary. France was eventually excluded — the four powers would occupy Germany, but only three would decide on reparations.

The idea expressed at Yalta, that the Soviet Union should receive half the reparations, met no resistance. More discussion arose over the shares to be given to other creditor countries. The United States was even prepared to suggest that the Americans and British should both be satisfied with 10 %, leaving 30 % for France and the other allies.

Understanding was reached on reparations to be paid to other allies on the basis of a Soviet suggestion. Under its terms allies of Germany during the war must submit their claims within a month to the Reparations Commission, which would then decide on the share for each creditor. These shares would be provided from the quotas of the three great powers. Half the reparations total was secured to the Soviet Union by fixing its share at 56 %, of which a part could be paid to some other country.

On the definition of the terms "reparations", "restitution" and "booty" agreement was not reached before the summit conference of the three great powers. For restitution the British on 7th July submitted a draft definition which the Americans approved. The Soviet Union on 13th July made its own proposal in which restitution was understood in a far wider sense than in the American and British draft.

On 5th July the Soviet Union promised to submit a draft definition of "booty" by the 11th, but when it did not arrive by that day the Americans submitted a draft of their own. The matter was not discussed, however, nor was the definition of "reparations".

The drawing up of a provisional reparations programme also remained unfinished. The Americans presented a draft, but there was time for only a brief discussion of it.

In Pauley's operational programme the last point concerned agreement on the principles for reparation management. Following

137) Clark Kerr from Moscow to FO 12.7.1945, FO371 45783 UE2962/624/77 PRO.

the instructions he had received Pauley on 22nd June made a proposal on this matter. At the beginning of July he informed Washington that after prolonged negotiations the delegations of the three powers had decided to recommend eight principles to their governments.

Recommendations

1. Removals of property for reparations shall be primarily such as to assist in bringing to an end the war-making power of Germany by eliminating that part of Germany's industrial capacity which constitutes war potential.

2. Reparations shall be such as will speed recovery and reconstruction in countries devastated at German hands.

3. For the purposes of making a reparations plan Germany shall be treated as a single economic unit.

4. Any plan of reparations shall be avoided which necessitates external financial assistance either to enable reparations deliveries to be made or to facilitate economic reconstruction required for reparations purposes or which might in the opinion of the governments concerned prejudice the successful execution of the task entrusted to the armies of occupation.

5. To a minimum extent reparations shall be taken from existing national wealth of Germany. While for convenience claims may be stated in money, it is necessary to bear in mind that in contrast to reparations after World War I which were assessed and exacted in money, this time reparations will be assessed and exacted in kind in the form of things such as plant, machines, equipment, stocks, foreign investments etc.

6. In order to avoid building up German industrial capacity and disturbing the long-term stability of the economies of the United Nations, long-run payment of reparations in the form of manufactured products shall be restricted to a minimum.

7. In justice to those countries occupied by the enemy, reparations shall be calculated upon the basis that the average living standards in Germany during the reparations period shall not exceed the average of the standards of living of European countries. (European countries mean all European countries excluding UK and USSR).

8. After payment of reparations enough resources must be left to enable the German people to subsist without external assistance. In working out the economic balance of Germany the necessary means must be provided for payment of imports approved by the governments concerned before reparation deliveries are made from current production or from stocks of goods.¹³⁸

Of the above recommendations the Soviet Union approved all except the last, which obliged Germany to pay for her imports before deliveries from current production or from stocks could be made. This absolute preferential treatment for imports meant in practice that payment of reparations would have been deferred to an unknown future date. The examples of Rumania, Finland and Hungary showed that it was not necessary to wait for the growth of an export surplus. From the Soviet viewpoint the attitude of the Western Allies seemed adverse to the reparations claim as a whole. While the war was still in progress the Americans and British had made some promise of compensation to the Soviet Union, but now this was in effect cancelled.

Separate attention must be given to the matter of what the Soviet Union was prepared to approve if all the recommendations had been fulfilled. Germany would have been treated as a single economic unit. What this would have meant in practice was not stated in the recommendations.

The Soviet Union was also willing for the main part of reparations to be in transfers of capital goods. In the proceedings of the Potsdam conference reparations from current production are not mentioned at all, and the recommendations did not reject such reparations in principle, though the amount involved was to be limited in practice. At the Moscow negotiations the Soviet was prepared to reduce its claim substantially from 20 billion dollars as a basis of discussion. But the Americans and British still required a plan with reasons given, which was awaited in vain in Moscow.¹³⁹

Soon after reaching its occupation zone the Soviet had started to move heavy industry, railways and other equipment as "booty". This had been done despite the fact that the Americans had bluntly prohibited such moves in the name of a "combined reparations

138) Pauley to SD 6.7.1945, FRUS Potsdam I, pp. 527—528.

139) T (Playfair) to FO (Dent) 17.7.1945, FO371 45783 UE3048/624/77 PRO.

policy".¹⁴⁰ The question of Germany's eastern frontier was also linked with reparations: if the Soviet Union wished to move the frontier further west in favour of Poland, the reduction of the area must be taken into account as weakening Germany's payment capacity.

Potsdam

At the first plenary meeting of the Potsdam conference Truman submitted a memorandum regarding Germany: this mentioned the seven reparations principles approved by the Allies in Moscow, and the eighth point as a proposal.¹⁴¹ The conference decided to leave preparation of the economic principles to be applied to Germany — including reparations — in the hands of the foreign ministers. The latter in their turn set up a sub-committee mainly composed of members of the Moscow Reparations Commission. The United States' delegation was, however, led by Assistant Secretary of State Clayton.

Before a decision on reparations the conference discussed a definition on "booty". On 21st July the Soviet submitted a draft whose second article described booty as "all supplies and equipment used by the enemy to satisfy his military needs and captured by the Allies before the end of the war on territories where military operations were conducted."¹⁴² In American and British opinion the Soviet definition was so broad that almost all goods found on German territory could be interpreted as booty. This was so far from the more limited view taken by the Americans and British that no compromise seemed probable. The Soviet Union wished to make sure of the goods to be obtained from Germany in case the reparations agreement came to nothing.

The Soviet definition supported their own policy in the occupation zone. The Americans and British observed more and more instances of light and heavy industrial equipment being moved by the Soviet authorities. If this continued the eastern zone

140) SD Memorandum (Bohlen) 7.5.1945, FRUS 1945 III, pp. 1209—1210.

141) First Plenary Meeting 17.7.1945, FRUS Potsdam II, pp. 52—53, 775—778, 832—835.

142) Proposal by the Soviet Delegation 21.7.1945, FRUS Potsdam II, pp. 846—847.

would be left with no means of paying reparations or maintaining the German economy. The Soviet Union would receive a certain quantity of goods while the western zones would receive no foodstuffs from the east.¹⁴³

The Moscow Commission had found no compromise between the Soviet and American-British views on German reparations. Following the open door policy the Americans wished to minimise reparations, but the Soviet Union could not approve any reduction of its claim to a fraction of the original. If the United States had started to negotiate on a reparations sum, the change in its policy since the Yalta conference would have been made public. The United States had to find a solution which would put aside Soviet claims without breaking the Yalta agreement.

The British and, in particular, the Americans wanted a reparations agreement with the Soviet government. Besides the Soviet Union many other allies had experienced the harsh occupation policy of Germany, and there would have been a good deal of sympathy for the Soviet in Europe and the United States if a disagreement between the great powers had come to light. For instance, the Soviet interpretation of booty was moderate compared with German practice during the war, and many European states would have supported the Soviet view. American political leaders believed that there was no point in competing over a suitable sum for reparations or a definition of booty. On the other hand it was in the American interest to reach something like an adequate agreement on reparations to prevent the accusation that they had forgotten the punishment of Germany. It was preferable for failure, if unavoidable, to occur in the practical application of agreed principles.

At the time of the Potsdam conference the Soviet Union in its occupation zone had adopted a policy of moving goods eastward without agreement between the Allies. The Western Allies could minimise the amount of reparations only by aiming at an agreement for each occupying power to collect reparations mainly from its own zone. Because each zone contained about as large a proportion of Germany's national assets as it had been planned to apportion to each power, division on a zonal basis was given

143) See e.g. Pauley to Truman 25.7.1945, FRUS Potsdam II, pp. 873—876.

growing American support.

The United States' proposal for distribution of reparations by zones was discussed unofficially by foreign ministers Byrnes and Molotov on 23rd July. Byrnes was surprised that the Soviet Union was able to link a reparations settlement with such factors as reduction of German territory by moving the eastern frontier and a broad definition of booty. Molotov admitted that Maisky earlier had not made the Soviet attitude to booty quite clear. Leaving this aside Byrnes continued that in order to avoid inter-allied disputes it might be worth while considering the division of reparations on a zonal basis. To supplement this an exchange of goods between zones might be considered.¹⁴⁴

Unofficial discussion between Byrnes and Molotov was immediately followed by an official conference of foreign ministers at which the Soviet Union submitted its own reparations plan.¹⁴⁵ It was a proposal supplementary to the Yalta agreement for approximately equal division of a total sum of 20 billion dollars between capital goods and current production deliveries. Transfers of capital goods for which assets within the frontiers of 1937 could be used, would be carried out within two years and current production deliveries within ten years of the surrender.

The Soviet Union also made a proposal for the administration of reparations deliveries.¹⁴⁶ A sub-committee of the Allied Reparations Commission was to be set up with members appointed by Britain, the Soviet Union and the United States. The Control Commission — with France included — would be kept informed of events, but would not play any part in actual decision-making. The Reparations Commission would make a list of industrial branches from which each occupying power might move equipment, and these removals together with others already made would be listed.

In this connection the foreign ministers discussed the practical carrying out of reparations procedures, reaching no conclusion but to send the matter to the sub-committee for preparation. Molotov tried to obtain from Byrnes and Eden a precise formulation of American and British ideas on reparation priorities in relation to

144) Byrnes-Molotov Meeting 23.7.1945, FRUS Potsdam II, pp. 274—275.

145) Proposal by the Soviet Delegation (s.d.), FRUS Potsdam II, pp. 863—864.

146) Proposal by the Soviet Delegation (s.d.), FRUS Potsdam II, pp. 864—865.

German consumption and imports. But attitudes remained as before.¹⁴⁷

In American thinking the question of defining booty was beginning to lose its significance. Because of wartime destruction and other reasons transfers of German national assets continued to be smaller than originally planned. The United States demanded that zone commanders be given responsibility for removals, whether reparations or booty. When Maisky submitted a proposal for a wider interpretation of booty, the Americans were in fact prepared to approve it. In their own zone the Americans could gradually cease the collection of reparations and if necessary take the goods they needed as booty.¹⁴⁸

On 23rd July the foreign ministers held another unofficial meeting.¹⁴⁹ Molotov submitted a new "true" Soviet definition of booty and admitted that the Soviet Union had moved equipment from Germany. He was also prepared to lower the Soviet claim. But Byrnes and Eden gave no ground at all, and the course followed from the Yalta agreement on had reached its end. On the other hand Molotov conceded the principle of collecting reparations by zones. The reparations sum still remained open, but Molotov expected the Soviet Union to obtain separate compensation from the Ruhr area.

As the conference continued the great powers tried to reach a settlement on the exchange of goods between the zones and the size of the compensation to be obtained from the Ruhr. But Molotov repeatedly returned to the point that the United States had changed its attitude since the Yalta agreement. In that agreement a fixed sum had served as the basis of discussion on reparations, but Pauley had announced that the Americans had abandoned this. Byrnes insisted that the United States had kept its promise, but in the light of events since Yalta a sum of 20 billion dollars must be considered "impracticable" — he avoided mentioning a suitable sum.

147) Sixth Meeting of the Foreign Ministers 23.7.1945, FRUS Potsdam II, pp. 276—281.

148) United States Delegation Working Paper 22.7.1945, FRUS Potsdam II, pp. 853.

149) Informal Meeting of the Foreign Ministers 23.7.1945, FRUS Potsdam II, pp. 295—298.

The true nature of the United States' proposal had not passed unnoticed by the Soviet Union, of course. Having failed to agree on reparations the Allies had to content themselves with what they could obtain from their zones without an agreement. From the Soviet standpoint the words of the Western Allies on reparations were meaningless and unsatisfactory. This was clearly apparent when after some delay in the discussion — elections were held in Britain, causing Churchill and Eden to be replaced by Clement R. Attlee and Ernest Bevin — Byrnes and Molotov met on 27th July. Molotov claimed openly that at Yalta the Americans had been on the Soviet side against Britain on the reparations question, whereas at Potsdam the Americans had taken the British side. Byrnes insisted that the United States had not changed its attitude — only circumstances had changed.

Molotov stressed the Soviet minimum demand, that it should receive goods transfers from the Ruhr.¹⁵⁰

Molotov confirmed this on 29th July, when bargaining over reparations continued, the British delegation having returned to full strength. Molotov officially announced that the Soviet Union agreed to the collection of reparations by zones. From the Ruhr the Soviet expected goods either to the value of two billion dollars or to the quantity of six million tons. In the opinion of Byrnes it was impossible to agree on a certain dollar value or tonnage, but the Soviet share could be 25 % of the total reparations to be taken from the Ruhr. This did not satisfy Molotov, who demanded a fixed sum of quantity.

The demand for a fixed sum arose understandably from the possibility that the Western Allies might make the total quantity of reparations so small that a quarter of it would be negligible. The express purpose of the Western Allies was to remove equipment connected with the war potential, but the amount of such equipment in the western zones was small, so small, in fact, that the Americans and British avoided making it public. Mention of a small sum during negotiations would probably have prevented an agreement.¹⁵¹

Molotov was justifiably anxious, too, that collection of

150) Byrnes-Molotov Meeting 27.7.1945, FRUS Potsdam II, pp. 449—452.

151) Pauley to Byrnes 28.7.1945, FRUS Potsdam II, p. 892.

reparations by zones might infringe the principle of treating all Germany as one economic unit. Byrnes held that the American proposal was not against this principle — it was merely a question of the method of collection.¹⁵²

Potsdam: a Lame Solution

The Potsdam conference was drifting into an impasse where disagreement on the frontiers of Poland was the central issue. The Americans did not wish to confuse opinion at home with a failed conference, however, and their wish to reach an agreement with the Soviet government on reparations was stronger than that of the British — it was preferable, after all, to break relations later over the practical interpretation of an agreement already made than to leave the conference with no agreement at all. But the British too agreed to goods transfers, mainly in order to ensure food supplies in their zone. The Americans were prepared for goods transfers to supplement a "zero solution" for the additional reason that the Soviet zone contained — calculations admittedly varied — less than half of Germany's total national assets. Also this American "openhandedness" would evidently cost nothing because it was doubtful whether the receiving states would be able to use the equipment moved from the Ruhr.¹⁵³

On 30th July Byrnes, an experienced politician, suggested that the Soviet Union agree to the American proposal for reparations and the Americans for their part agree to hand over the areas east of the Oder-Neisse line to Polish administration until a peace treaty was made with Germany. As part of Byrnes' suggestion 25 % of such industrial equipment as was not indispensable for the peacetime economy would be moved from the Ruhr to the Soviet Union on condition that foodstuffs, coal and other commodities of corresponding value were moved from the Soviet zone to the West. In addition 15 % of such equipment from the Ruhr would be moved without counter-deliveries. In the situation which then

152) Pauley to Maisky 27.8.1945, FRUS Potsdam II, pp. 893—897.

153) Clayton to Byrnes 29.7.1945, FRUS Potsdam II, pp. 900—901, Pauley to Byrnes 30.7.1945, FRUS Potsdam II, p. 917.

prevailed the United States' suggestion signified progress, and Molotov promised to convey it to Stalin. True, Molotov at once seized on the question of who should decide what equipment was suitable for reparations and demanded Soviet participation in this through the Control Commission or the Reparations Commission. Molotov also wished the agreement to mention a fixed dollar sum. A third problem would be constituted by deliveries from the Soviet zone.¹⁵⁴

On 30th July the British made their own proposal on goods transfers.¹⁵⁵ Under its provisions the Soviet Union would have obtained 10 % of the equipment suitable for reparations from the Western zones and particularly from the Ruhr. On the other hand transfers between the zones would not be made, as this would give reason for inter-Allied disputes. Treatment of all Germany as an economic unit would enable its various parts to be equally provided for.

Molotov at once presumed that the American proposal was nearer to the Soviet view. This was partly because in Bevin's opinion the commander of the zone concerned should decide what equipment was suitable for reparations — and in the case of the Ruhr he was British. Molotov suggested an addition to the agreement — the words "and the Control Commission". Bevin agreed to this, but did not promise the power of final decision either to the Control Commission or to the Reparations Commission.

At a general session on the last day of July Stalin formally rejected the idea of linking extraneous matters to a reparations settlement. He now submitted a proposal for an agreement on reparations.¹⁵⁶ This approved the collection of reparations by zones and the exchange of goods as follows: 15 % of assets to be removed from Western zones — not only from the Ruhr — should go to the Soviet Union in the course of five years in exchange for the same value of goods, also 10 % of the assets in question without exchange. The amount of assets to be removed would be determined by the Control Commission after a statement by the

154) Byrnes-Molotov Meeting 30.7.1945, FRUS Potsdam II, pp. 480—483.

155) Proposal by the British Delegation 30.7.1945, FRUS Potsdam II, pp. 920—921.

156) Proposal by the Soviet Delegation (s.d.), FRUS Potsdam II, pp. 1593—1594.



Ernest Bevin who replaced Sir Anthony Eden as Britain's Foreign Secretary.

Reparations Commission. On the part to be played by the zone commander and the participation of France in the Reparations Commission the Soviet proposal, had nothing to say. But it suggested that the Soviet Union receive additionally 500 million dollars' worth of shares in industrial and transport enterprises in Western zones, 30 % of German foreign investments and 30 % of German gold which had come into Allied possession. The Soviet Union was prepared to pay out of its own share the reparations due to Poland, and the United States and Britain should pay out of their own shares the reparations due to France, Yugoslavia, Czechoslovakia, Belgium, Holland and Norway.

In the course of discussion Stalin wished to confirm a time within which the equipment to be moved should be defined. He suggested three months, but this was lengthened to six months at Bevin's suggestion.

The Soviet proposal signified more goods transfers to the East than had been mentioned in the United States' proposal, in addition to which German shares and gold were suggested as reparations. Truman asked Stalin to be satisfied with the equipment transfers proposed, and to leave out shares and gold. To this Stalin agreed, while Bevin, negotiating for Britain, yielded to Truman's compromise very reluctantly.

In the negotiations French membership of the Reparations Commission was confirmed, as well as a formulation of an agreement with those other states entitled to reparations that had not been mentioned, that is, apart from Britain, the Soviet Union and the United States.

Potsdam: Italy

At the Potsdam conference the United States gave particular attention to regulation of the Italian question. During the occupation period its aim was to ensure by various means that Western democracy was implanted in Italy and its continuance guaranteed by helping the country to self-sufficiency and economic independence as soon as possible after the war. Although American interests in Italy had not been especially great, Washington did not wish to forget them altogether. The American share in the occupation was felt to be — not least among the Italian and Roman Catholic section of the American population — mainly a liberation from the power of Nazism and a return of the lost sheep to the flock.¹⁵⁷

Reparations did not suit the picture of a recovering, independent Italy, a participant in the open door policy. For the purposes of the Yalta conference Washington had decided on a principle which allowed off the suspension of a decision on Italian reparations until the peace conference.

In the opinion of many Britons the Americans had almost entirely forgotten that Italy had been the Fascist ally of Germany which had attacked the British and changed sides in the war only to avoid the consequences of military defeat. The American view was that the British — wishing to keep Italy in subjection — had not broken free of their former imperialistic notions.¹⁵⁸

By the time of the Potsdam conference it was clear to the Americans that the political position of Italy would not serve as a basis for her to take advantage of American economic aid. For this reason Byrnes proposed at the beginning of the conference that

157) See e.g. Briefing Book Paper (s.d.), FRUS Malta and Yalta, pp. 276—283.

158) Woodward 1976, p. 467.

surrender terms be replaced by an undertaking from the Italian government to observe certain regulations before the peace treaty. Italy would still be obliged to pay reparations.¹⁵⁹

When the American proposal came up for discussion, Stalin linked the Italian peace treaty with similar treaties for Bulgaria, Rumania, Finland and Hungary. The most urgent work of the Council of Foreign Ministers which had been formed proved to be the Italian treaty, but the preparation of treaties with the other countries concerned also devolved on the Council. The three great powers at Potsdam also agreed on the principle that Italy and the other countries could be members of the United Nations.

At a foreign ministers' conference on 20th July Molotov brought up the Italian reparations liability. Byrnes and Eden thought that Italy had not the means of payment, but they did not deny the obligation in principle. Byrnes remarked that the United States government had already given Italy some 200 million dollars in aid and would be obliged to give a further 400 or 500 million during the coming winter. For this reason, in the American view, reparations were not an immediate problem in settling the Italian question.

Molotov was able to use the example of Finland to advantage: could the world consider it justified for Finland, a small country, to pay large reparations while Italy, a large country, paid nothing?

Eden bypassed Molotov's statement by asking him on the basis of his previous statement what connection there was between reparations and membership of international organizations. Reparations would be arranged as part of the peace treaty and had no wider importance. Molotov observed that members of the United Nations would not pay reparations. The question of United Nations membership and reparations remained partly open, though later both Eden and Molotov demanded that peace treaties — including their reparations articles should be signed before the countries concerned could enter international organizations.

At a general session on the same day, 20th July, Truman again briefly indicated that the Americans did not intend to give large sums of money to European states — when thinking of Italian reparations it was as well to remember that during the following

159) Briefing Book Paper (s.d.), FRUS Potsdam I, pp. 681—683.

winter the United States would use from 750 million to a billion dollars for feeding the Italians. Countries which were the objects of aid must be made self-sufficient.

Discussion took a new turn when Molotov at a foreign ministers' meeting on 24th July made a proposal on reparations for both Italy and Austria. In this proposal it was said that Austria was able to pay 250 million dollars' worth of reparations in six years, and Italy 600 million. The Soviet Union drew special attention to the fact that these countries no longer had military expenditure. These suggestions were left to be dealt with by the economic subcommittee formed earlier.¹⁶⁰

But the sub-committee made no progress. The Americans and British could not consent to reparations from current production as long as Italy and Austria had to be assisted. At a meeting of foreign ministers on 27th July all that Byrnes could imagine as attainable in Italy was "removal of machinery and equipment from war industries, provided they had no peacetime use." To Molotov this was quite inadequate. Again he insisted that countries which had occupied Soviet territory must not come out of the war unpunished. Rumania was paying reparations — it was incomprehensible that the Italians and Austrians should not pay. The Rumanian armistice agreement was signed by both Britain and the United States — in the case of Austria he could understand the Americans giving up their reparations claim; the Austrians had not occupied United States territory.

Byrnes appealed to the practical aspect. If a country could pay reparations it did not need help from UNRRA. Molotov could not approve such a stipulation for the work of UNRRA. The foreign ministers, in fact, could agree on nothing but to record differing opinions for the plenary meeting. At this meeting on 28th July Stalin began with a compromise: because Austria had had no army of her own in the war the Soviet Union was able to give up its claim for reparations from Austria. Italy on the other hand had sent her army to the Volga, and her liability to pay reparations could not be abandoned. Truman did not yield in the slightest. If Italy was able to pay he had nothing against it. Stalin reminded him that the United States had agreed to transfers of equipment and asked

160) Proposal by the Soviet Delegation 24.7.1945, FRUS Potsdam II, p. 666.

how much of such equipment there was. In this connection Stalin wished a fixed dollar value to be agreed upon.

Truman replied that he could not state a value at that moment, and Stalin agreed to await an answer. The British hastened to Truman's aid. Attlee and Bevin learned by questioning that Stalin wished to obtain from Italy the same sort of military equipment as from Germany. Because this could not be particularized for the moment, the Soviet wished some fixed sum for reparations to be appointed — Stalin was prepared to discuss a reduction of the original sum. Bevin demanded that Italy first pay for assistance received from the United States and Britain, while Stalin demanded that the aggressor pay for at least part of the destruction he had caused. The question remained open when the plenary meeting ended.

At a meeting of foreign ministers on 30th July both Bevin and Molotov submitted proposals. The British did not demand reparations from Austria, and the Control Commission would later determine the equipment and other goods to be transferred as booty or otherwise.¹⁶¹ The Soviet government proposed that Italy and Austria be obliged to pay reparations in the form of important military equipment within one year. The Austrian Control Commission would fix the final sum.¹⁶² Byrnes' opinion was that Italian and Austrian reparations had long been discussed, but no agreement was in sight. If Molotov still wished to return to the subject he could do so at a plenary meeting. Molotov did not, however, and the matter was discussed no further at Potsdam.

The Americans had several reasons for opposing Italian reparations. First, the dismantling of industry affected the Germans primarily, whereas the Italian industrial potential had not proved dangerous. Without reparations Italy could be more quickly linked to an economic system in accord with American ideas. In addition the United States Italian population would hardly have looked favourably on harsh treatment of their homeland.

The discussion begun at Potsdam continued at a conference of foreign ministers in London during September 1945. The Soviet

161) Proposal by the British Delegation 30.7.1945, FRUS Potsdam II, p. 666.

162) Proposal by the Soviet Delegation 30.7.1945, FRUS Potsdam II, p. 667.

Union repeated its demand for 600 million dollars' reparations. When Britain and the United States considered this too much, Molotov was prepared to reduce the sum to 300 million provided the Western Allies relinquished their shares. Of the reduced sum 100 million belonged to the Soviet. On this basis the council of foreign ministers composed a draft Italian peace treaty which came up for discussion at the Paris peace conference.

Molotov, however, could not regard as justified the British and American attitude to the Italian reparations liability as a whole. He reiterated that small countries such as Rumania and Finland were paying 300 million dollars, and it was therefore questionable policy to allow a great power such as Italy to escape without a similar payment. The case of Finland in particular showed the need to advance from the experiences of the First World War to new models which had proved fully satisfactory. Bevin, the British Foreign Secretary, observed that his country had agreed to the reparations clauses for Rumania and Finland only with reluctance and with the proviso that they should not serve as precedents. Italy would not be able to pay reparations, which would be shifted to the shoulders of British taxpayers. Byrnes agreed with Bevin's principles. No progress was made in the regulation of Italian reparations, the further treatment of which awaited the assembly of the Paris peace conference.

Forward from Potsdam

As mentioned earlier, the Potsdam agreement provided that equipment to be moved from Western zones as reparations should be defined within six months of the signing of the agreement. This was the task of the German Control Commission which was obliged, in making its reparations plan, to take note of the economic principles affecting Germany which had been agreed at Potsdam.

The commander of each zone had final responsibility for deciding what goods were moved. Among the Americans, accordingly, General Clay and his subordinates played the main part while Pauley withdrew from the handling of German reparations. His talents as a negotiator were to be put to use in the settlement to be made with Japan.

In conjunction with the Potsdam conference the Moscow Reparations Commission moved to Berlin, though an official decision was not made until 25th September 1945 at the London conference of foreign ministers. France was formally invited to be a member, but in practice the Control Commission made the main decisions on reparations. The Western powers established the Inter-Allied Reparations Agency (IARA) which met in Paris and whose function it became to allot the reparations payable from the occupation zones of Britain, France and the United States to the receiving states. Agreement on this was reached on 21st December 1945. Relations between IARA and the Control Commission remained undefined in many respects, which caused friction.¹⁶³

German Production Level

In the United States the Potsdam settlement was seen to a great extent as a complete solution to the German reparations problem. And Pauley's removal from the German issue signified a move from political decision-making to the executive level.

A sign of this change was the American attitude to Finland. In March 1945 parliamentary elections in the style of Western democracy had been held in Finland, and in the summer Finland established diplomatic relations with all the great powers. Because in Finland — unlike Rumania and Hungary — political life was settling down in a way which satisfied the Americans, Washington at last bowed to repeated Finnish request for negotiations on credits. Early in 1946 these discussions led to the granting of credits.¹⁶⁴

These credits were intended for the needs of the woodprocessing industry directed to Western markets. Although reparations industry was left outside the credits, the dollars granted brought indirect relief to the discharge of this obligation. The decision on credits meant a change in the American policy of not granting such help to countries paying reparations. In Washington's view,

163) Clay to War Department, Sept. 1945, Papers of General Lucius D. Clay I, pp. 72—74. The IARA Agreement 21.12.1945, Ratchford & Ross 1947, pp. 231—241.

164) See Heikkilä 1982.

solution of the German reparations problem was so far removed from other cases that it was unaffected by the change of principle involved in allowing credit to Finland.

Transfers of goods under the Potsdam agreement were not very large in quantity. The main problem was whether the members of the Control Commission could reach agreement on what goods to transfer. Representatives of the four countries were obliged to accept strict interpretations of the Potsdam terms, agree on the capacity of Germany's remaining industry, indicate the equipment to be removed as reparations and finally distribute it to each receiving state. This in turn led to the discussion of even more extensive matters such as the forming of a central administration for Germany and the making of an export-import programme.

In the principles approved for Germany, which were based largely on earlier American recommendations in Moscow, it was noted the except for goods transfers mentioned in the reparations agreement "payment of reparations should leave enough resources to enable the German people to subsist without external assistance" and that a living standard should be maintained in Germany "not exceeding the average of the standards of living of European countries. (European countries to mean all European countries excluding the United Kingdom and the Union of Soviet Socialist Republics.)"

Thus the assessment of German reparations was directly linked with regulation of the country's living standard, over which the representatives of the four powers clashed having differing viewpoints. The Soviet starting-point was that equipment providing an average European living standard need not be left in Germany — the Potsdam agreement was sufficiently fulfilled if equipment was dismantled to a standard somewhat below the average. Next, Soviet representatives counted all goods produced as part of the living standard; each product group must be separately examined and if necessary brought down to the average standard of the rest of Europe on the per capita principle.

The Americans and British, for their part, viewed the concept of living standard as one whole. Because certain fields of industry were dismantled almost entirely and in certain others there could be no production whatever, for instance through lack of raw materials, production in some fields had to exceed the European average if an average living standard was to be achieved. Behind

this lay the understandable fear without substantial production in some field the Germans would not be able to pay for their indispensable imports. Correspondingly the Soviet Union wished to expand the number of assets included in reparations.

After negotiations at many stages the representatives of the four countries agreed that each of them should submit a proposed reparations plan by mid-January, a time limit later extended to the beginning of the following month. It was finally possible to start negotiations for the accordance of these plans.

Naturally the amount of steel production had a decisive influence on the quantity of equipment remaining for reparations and on the German living standard. A draft on this matter was prepared by the Level of Industry Committee, an administrative organ set up by the Control Commission, which held its first meeting on 18th September 1945. Its work, as a matter of fact, consisted largely of theoretical planning. The committee talked of a German annual steel production of 5—9 billion tons at a time when German industry fell far behind this. It was estimated at the time that at least four years must be allowed before the planned ceiling could be reached. Also discussed were German exports amounting to three billion marks when the actual exports in 1946 came to 600 million. The practical aim was within a few years to reach a level above which anything remaining could be transferred as reparations.

On 10th January 1946 the Allies in fact reached agreement that 5.8 million tons annual steel production should be the aim and 7.5 million tons annually the ceiling for the expansion of German steel production. But the four powers soon disagreed on whether 5.8 or 7.5 million tons annual production should be the starting-point for calculations of the level of Germany's other industry. The Soviet Union, France and the United States supported the smaller amount, while the British remained alone in favour of the larger.

As a production ceiling for various goods the Soviet generally proposed the lowest level, while General Clay aimed at a compromise with the high figures suggested by the British. Later Clay was criticised for having agreed too quickly with Soviet views. For steel the Soviet ceiling had been 4.6 million tons, but Clay had caused it to be raised to 5.8 million. Although the original American proposal was near that of the British, Clay thought he had gained such a large concession from the Soviet government

that the British must be induced, on the strength of Washington's support, to approve it. Clay wished for collaboration with the Soviet Union but also wished to avoid departing too far from the aims of the Potsdam agreement. Also it was worth reducing steel production, for this would enable the output of light industries to be increased.¹⁶⁵

Clay's efforts to achieve a compromise were endangered when France asked what the production possibilities of Germany would be if the Saar territory were joined to France. Clay answered at once that the United States could not deal with reparations on that basis because the Potsdam agreement had directed that Germany be treated as a single economic unit. Separation of the Saar immediately affected the possibilities for the payment of reparations. The Soviet Union agreed that the matter was already settled: territorial arrangements had been agreed at Potsdam, and Germany remained an economic unit. The British, on the other hand, were prepared for the clarification proposed by the French even if the conclusions to be drawn from it were outside the powers of the Control Commission.¹⁶⁶

On 18th February France asked officially for the Saar territory to be placed permanently under French administration. She announced at the same time that she could not approve the establishment of a German central administration before the Ruhr area was put under international control. The Western powers were left in suspense, waiting to see on which side the Soviet Union would cast its lot: Germany and her communists expected their country to remain as before, while the French government with communist support worked for the separation of the Saar.

The Saar was of little economic importance to the Level on Industry Plan which was in preparation. In this connection the Ruhr was far more important.¹⁶⁷

After many stages of negotiation The Final Reparations Plan — the Plan of the Allied Control Council for Reparations and the Level of the Post-War German Economy — was signed on 28th March 1946. Despite the title, this contained no direct agreement

165) Clay to War Department and Byrnes 31.1.1946, Papers of General Lucius D. Clay I, pp. 154—155. Paterson 1975, pp. 240—242, 253—254.

166) Clay to Hilldring 1.2.1946, Papers of General Lucius D. Clay I, pp. 156—157.

167) Clay to Hilldring 6.3.1946, Papers of General Lucius D. Clay I, p. 176.

on reparations whatever. But it gave a starting-point for Germany's future production: prohibited and limited fields of industry were defined, also the general level of industry and the value of exports and imports. Finally the agreement stated that at the next stage settlements must be reached "on disarmament, reparations, the post-war German economy and the German balance of trade." Once again the most difficult questions were bypassed, with the result that this agreement, like others, left several problems unsolved. There was no mention even of when the agreement would come into force and how long it would remain in force. As will be made clear later, this was of no practical importance, because reparation transfers ended only a few months after the agreement was signed.

Unmentioned too were reparations from current production. The Americans and British firmly believed that the industrial level which was planned was insufficient for such deliveries. In several connections the French stressed that they wished productive capacity to be left for this purpose. The Soviets wished productive capacity to be as low as possible, but did not commit themselves with regard to production for reparations. The Soviet Union wished to return to this matter at a later stage.

The Americans and British left the other Allies in no doubt that they had no wish for difficulties to be caused in Germany by too heavy a reparations programme. In the final stage of negotiations at the beginning of March 1946 the Americans announced: "it is the U.S. position that there should be no removals of capital equipment as reparations from the light consumer goods industries necessary to sustain a peacetime economy." But the agreement did not mention how reparations were to be obtained from these or from unrestricted fields of industry. The American and British standpoint was that reparations could not be received from these fields at all, while the Soviet Union and the French believed the opposite.

Deadlock on Removals

The aforesaid Level of Industry Plan placed a ceiling on German production in various fields, but some dominant aspects of German economic life were still unsettled: without a central



General Lucius D. Clay, Commander of the American zone in Germany. This photograph was taken in 1961 when he was on the way to Berlin to be president Kennedy's Personal Delegate there.

administration, for instance, Germany's economic life as a whole could hardly be controlled, and without an export-import programme not even the Level of Industry Plan could be carried out. France could not agree to the creation of a central German administration, however, before the decision she wished for had been reached on the Ruhr and Saar issue. The Soviet Union for its part demanded a reparations agreement before an export-import programme. Great power collaboration was undermined by uncertainty as to whether a concession made over one matter might prove ineffective in solving other problems.

As long as German economic integration was not practically realized — and with it the organization of Western Zone food supplies — the Americans and British were not satisfied with the situation. When France and the Soviet Union showed no wish to assent, Clay on 4th May ordered reparation transports from the American zone to cease except for the removal of 24 installations which had already been carried out in advance. Clay's foremost anxiety was the lack of raw materials and foodstuffs in the American occupation zone. It was clear to him that if the Soviet

Union offered food, communism might well spread throughout Germany. Revival of Germany on a moderate scale, including currency reform and, at the least, union of the American and British zones, would lay the foundation for a stabilization of German political affairs. On the other hand, the share of factories and equipment allocated for reparations in the reconstruction of Europe and Germany was so small in Clay's opinion that it provided no justification for not carrying out the Potsdam agreement with regard to the dismantling of Germany's war potential.

Clay had a conviction which now seems naive that the signatories of the Potsdam agreement — Americans, British and Soviets — would finally reach unanimity with the help of negotiations. But the French, who had become involved later, showed no real understanding of the significance of Potsdam.¹⁶⁸

General Clay decided to break off reparations deliveries without any order from Washington, where, although the German question was viewed from another angle, the zone commander's decision suited the aims of the political leaders also. It was calculated in Washington that a policy of collaboration, mainly through the United Nations, the American monopoly of atomic weapons and the country's economic power would provide sufficient foundation for maintaining their leading position throughout the world. By the spring of 1946 when the Soviet Union seemed reluctant to bow to the will of the United States, the Americans began to speak in sharper tones.

It was understood in Washington — but not by Clay — that to Europeans and many American minority groups the main issue in international politics was not a contest between communism and democracy. In Europe the liquidation of fascism and its legacy was primary. Secretary of State Byrnes in particular wished to ensure that peace treaties with Italy, Bulgaria, Rumania, Finland and Hungary were concluded. There was also a wish to see how Europeans would perform in elections following the period of fascism and national socialism. On the other hand a swift and extensive reconstruction of Europe would have aroused

168) Clay to Eisenhower 26.5.1946, Papers of General Lucius D. Clay I, pp. 212—217. LaFeber 1968, p. 32.

resentment in the United States and Europe alike, which in turn would have increased the support for communist parties in various European countries.

The basic British aim in Germany was simiral to the American. The spread of Soviet influence and with it communism — and equally the spread of extreme right-wing ideas and movements — were to be prevented by restoring to Germany an adequate living standard with a democratic system of administration and justice. Accordingly the British were glad to establish connections with Germany's Social Democratic Party and trade unions. It was not, however, primarily fraternal feelings that initiated these gestures by the Labour Government but rather their fear that these channels might be used by the Soviet Union for its own influence over the Germans.¹⁶⁹

169) See Rothwell 1982.



European Countries concerning Reparations, 1943–1947.

Reparations as Part of Peace Treaty

The Paris Conference of Foreign Ministers

At the Potsdam conference it was decided to set up a Council of Foreign Ministers for the purpose of preparing peace treaties with Germany's European satellites — Italy, Rumania, Bulgaria, Hungary and Finland. Five foreign ministers were scheduled to meet on 11th September 1945 in London, but when their conference ended on 2nd October very little had been achieved.

In London reparations were discussed in conjunction with the peace treaty to be made with Italy. The Soviet Union proposed a payment of 600 million dollars. The United States and Britain took the view that such an obligation would make the country dependent on foreign aid. Molotov was prepared to reduce the sum to 300 million, the Soviet Union taking 100 million and Yugoslavia, Greece and Albania sharing the rest. Rumania and Finland were paying similar amounts, and a country such as Italy could therefore do the same. Bevin reminded the others that Britain had assented only with reluctance to the mention of a reparations sum in the agreements with Rumania and Finland — and with the stipulation that these cases should not be taken as precedents later. Byrnes agreed that the experience of the First World War showed the danger of heavy reparations. Molotov preferred to make use of later experience: Finland with a population of four million was paying 300 million dollars on the basis of a mutual understanding with the Soviet Union, and the same should not be impossible for Italy. No further progress was made over Italian reparations, which were reserved for later discussion.

The deadlock in which the London negotiations ended was a disappointment to all parties. The process of untying the knot began in Moscow, where the foreign ministers met on 16th December 1945. It was decided that the deputy foreign ministers should prepare draft peace agreements with Italy, Rumania, Bulgaria, Hungary and Finland. After completion of these drafts the Council of Foreign Ministers would meet not later than 1st May in Paris, when the 21 states which had fought against the Axis in Europe would be invited. On 25th April in Paris the foreign ministers of the four most important Allies met for the purpose of carrying forward the preparatory work of the deputy foreign ministers. It was clear at this stage that the 21-state conference could not open at the beginning of May.

Byrnes soon had to alter his belief that the Soviet Union would eventually bow to the United States proposals on the main issues. For three weeks the foreign ministers negotiated with no progress being made on the central questions until they decided to intermit the conference, leaving the deputy foreign ministers to continue preparations. The foreign ministers returned to Paris in mid-June. It was only gradually and by way of unofficial talks that decisions were approached. The first sign of disentanglement was Molotov's announcement on 27th June that the Soviet Union agreed to the frontier line proposed by the United States between France and Italy. Molotov was also prepared to accept the United States proposal on Trieste provided the Soviet received reparations from Italy in the form of goods deliveries to the value of 100 million dollars. The Western powers approved this on the condition that the Soviet supplied Italy with the raw materials needed for reparations and agreed to the holding of a 21-state peace conference on 29th July for the purpose of deciding the share of Italian reparations to be received by the other Allies. This meant a clear breakthrough which was to lead to an agreement on all European reparations except those from Germany.¹⁷⁰

170) Polvinen 1986, pp. 205—208.

A Soviet Proposal

Clay's decision to break off advance deliveries of reparations brought negotiations on Germany to a stage where it was beyond the authority of the Control Commission to arrive at a new settlement even in principle. In Paris the foreign ministers continued negotiations on the German question as on others, and here Molotov on 9—11th July offered a new opportunity for reaching agreement.¹⁷¹

Molotov did not miss the opportunity of condemning Clay's decision to break off deliveries. He recalled the original Soviet demand for 10 billion dollars' worth of reparations in the form of transfers of capital goods, deliveries from current production and German manpower. At Potsdam transfers of capital goods had been agreed, but Clay had broken off advance deliveries before a final agreement on transfers had even been made.

Molotov's condemnation of American policy was not surprising. But his views on the revival of the German economy were something new. Germany, he thought, formed an important sector of the world's economy, and to destroy her in an economic sense or turn her into a predominantly agricultural country served no one's interest. A vengeful peace would only give the Germans reason for another military and economic resurgence. But a controlled development of peaceful productivity — after total disarmament (military and economic) and strict four-power supervision of the Ruhr — would be of benefit to the parties concerned.

The Control Commission had imposed a ceiling on German production which had by no means reached at this stage. Despite this the Soviet Union was prepared to raise that ceiling provided that the increased output was used for peaceful purposes and an increase of trade. "The adoption of a corresponding program for the development of German peaceful industries which will provide for the development of foreign trade of Germany as well as for the establishment of an interallied control over the whole of German industry satisfies the need for the implementation of the decisions of the Berlin Conference which provide for the treatment of Germany as an economic whole."

171) Molotov's statements, FRUS 1945 II, pp. 642—847, 869—877, 880—887. Paterson 1975, pp. 255—256.

Molotov's statements differed clearly from the principles expressed by Varga. In its own occupation zone the Soviet Union had observed that reparation transfers of capital goods did not pay if carried to extremes. For this reason the Soviet government now demanded deliveries from current production, to take the form of a certain percentage of the output of specific factories. This principle the Kremlin was ready to extend throughout Germany. On this basis Germany would be able to start expanding her production. Molotov no longer said, like Varga, that the German living standard should remain lower than the Soviet one.

In Paris, however, the Western Allies had made all the concessions to the Soviet Union that they were prepared to make. Byrnes and Bevin branded Molotov's statements as a blatant attempt to obtain more reparations while the Soviet government posed as the champion of a united and prospering Germany. Byrnes and Bevin eagerly seized of the criticism concerning the ending of the removals of goods, which led to discussion of the problems arising from payment of reparations by these deliveries alone. They continued to stress that if a surplus appeared in any zone it should be put to general use, and that imports should be paid for by the exports of all zones. This meant that the Soviet Union would have had to give up the principle enunciated by Molotov.

The Western view was that Germany must produce an actual surplus before she could pay reparations, while the Soviet Union felt that reparations from current production and reconstruction could be made complementary. By summer 1946 there was a settled conviction in Washington and London that by means of reparations — as a part of wider aims — the Soviet Union was trying to extract as much as possible from Germany, while according to Western ideas reparations from Germany were in practice impossible. But it should be mentioned separately that the Western powers at this stage regarded reparations from current production as by no means forbidden in principle — it was merely that the necessary conditions were absent.

After their fruitless talks on Germany and Austria the foreign ministers ended their conference on 12th July, and the peace conference of 21 states was at last able to start at the end of that month. The first weeks were spent in rhetorical opening speeches by the Allies, after which, from 10th August onward, the losers

were given a chance to express their views. After some general discussion the peace conference was divided into five political and territorial commissions, a combined military and a combined judicial commission, as well as two economic commissions, one dealing with Italy, the other with the Balkans and Finland.

Paris: Deputy Foreign Ministers

In themselves the reparations programmes for Rumania, Finland and Hungary could be accomplished without exerting pressure for changes in the reparation articles of the armistice agreements. And in the case of Finland there were no other reasons for change. On the last day of March 1946 the Soviet Union submitted the draft of a peace treaty with Finland.¹⁷² Its seventh article dealt with reparations and was similar to a corresponding provision in the armistice agreement, although a two-year extension of the compensation period allowed by the Soviet Union at the end of 1945 was taken into account. No changes were made in the treatment of the reparations article by the assistant foreign ministers — it was merely submitted to the Council of Foreign Ministers in the form proposed by the Soviet Union.

The unanimity which had prevailed in the case of Finland did not continue when the articles dealing with Rumania and Hungary was considered. The failure to regulate German reparations had given new meaning to the reparations question in terms of great power politics. On 21st June at a conference of deputy foreign ministers the United States delegation submitted a proposal for a peace treaty with Hungary. The early part of its reparations article was in accord with the Soviet proposal, but there was also a proviso which was explained. The United States delegation reserved the right to bring up this question again at the peace conference. In the explanation it was mentioned that the United States had reserved a similar right in the armistice agreement with Hungary in case American interests were injured later.

The Americans had already declared their anxiety over the weakening of economic conditions in Hungary, and when this

172) Draft Peace Treaty with Finland. Proposed by the Soviet Delegation 31.3.1946
C.F.M. (D) (F) (46) 1, FO371 57156 U3717/69/79 PRO.

appeared to be threatening even a minimum living standard they suggested on 2nd March that the situation in Hungary be examined. In Paris the United States renewed its proposal for the setting up of a commission to do this.¹⁷³ Although the United States' initiative did not lead to noteworthy results it was a sign to the Soviet Union of American efforts to reduce the part played by reparations in economic dealings.

The Soviet Union did not accept the proviso with its explanatory note for a draft treaty. The British delegation suggested a compromise whereby the United States' proposal as a whole would be included in the text in English, while the Russian text would contain the proviso without the explanation. Deputy foreign minister Gusev agreed to this on condition that the Hungarian gold and other property in Allied hands be mentioned in the draft. During the war the Germans had appropriated Hungarian assets, and most of these were found to be in the American occupation zone when the war ended. It was in the American interest, naturally, to play down the amount of these assets and to stress the importance of easing reparations, whereas the Soviet and Hungarians in various connections stressed the importance of returning the assets for the country's reconstruction.

On 27th July, however, the Soviet Union announced a change of attitude, stating that it could not approve the inclusion of the American proviso and explanation in any printed draft agreement to be submitted to the peace conference. After long discussion the deputy foreign ministers decided to distribute draft agreements for Bulgaria, Italy, Rumania and Finland to the peace conference, but kept back the draft for Hungary until agreement should be reached on it. It was finally agreed that the proviso without explanation should remain in the draft agreement.

Paris: Speeches by the Losers

Rumanian reparations came to the fore when the former enemies were given a chance at the peace conference to give their views on the proposed agreements. Foreign Minister George Tatarescu,

173) Dunn from Paris to SD 19.7.1946 and footnotes, FRUS 1946 III, p. 5.

president of the Rumanian delegation, spoke for his country on 13th August. In respect of Rumania's reparations to the Soviet Union he suggested no change. The Soviet Union, said Tatarescu, had limited its demand to one fifth of the destruction caused by Rumania. On this basis he hoped that others too would treat Rumania favourably and return property which had been removed from her territory.¹⁷⁴

Tatarescu had exposed his flank, and Byrnes did not fail to take advantage. He told Tatarescu that he had received the impression that "the only way to be considered generous was to take something from Rumania." Tatarescu explained that he had not intended to deny that the United States too was generous. However, during the war Rumania had destroyed a great deal of Soviet property and the Soviet had not demanded full compensation, contenting itself with 300 million dollars.

Byrnes replied that it was strange to thank people for not taking everything. It was wrong, he thought, to calculate compensation on the basis of property destroyed without taking account of human life lost. American demands on Rumania had increased mainly because of dealings in oil. The Rumanian government wished oil to be treated as part of reparations, paying the companies concerned a fixed price which the Americans thought too low. Tatarescu said he was aware of the situation and pointed out that British, Italian and Rumanian companies were receiving the same price. Despite this the oil companies were not in an unfavourable position but were prospering.¹⁷⁵

On 14th August Foreign Minister Janos Gyöngyösi, leader of the Hungarian delegation, gave his country's views on the draft agreement. There was no mention of reparations payable to the Soviet Union.¹⁷⁶ In written statements by the Rumanian and Hungarian delegations there was also no reference to the reparations article.

In general discussion after the Hungarian declaration the issue of compensation caused disagreement between the great powers.

174) Fifteenth Plenary Meeting, August 13, 1946 4 P.M., FRUS 1946 III, pp. 190—198.

175) SD Memorandum (Matthews) 29.8.1946, FRUS 1946 VI, pp. 626—632.

176) Seventh Plenary Meeting, August 14, 1946, 4 P.M., FRUS 1946 III, pp. 210—220.

Byrnes stoutly defended the economic aims of the United States and accused the Soviet Union of breaking agreements by keeping the countries of eastern Europe under its own supervision. The United States, he said, had given and was still giving substantial economic help in various forms, whereas reparations meant the removal of foreign exchange and goods from the countries in question.

In his reply Vyshinsky concentrated on the Hungarian situation. The Soviet government had made a justified demand but had shown flexibility in order to find a practical solution. Of the agreed 35.5 million dollars Hungary had delivered only 10.5 million or about 35 %. In the exchange of goods between the countries, moreover, Hungary had received commodities from the Soviet Union to an extent which reduced the Soviet compensation to a mere 3.5 million dollars. Despite this his country had fulfilled its undertaking and even granted two years' extra time for payment of reparations. Byrnes, observed Vyshinsky, had forgotten to mention that the Soviet Union had not only contented itself with partial payments but had also given economic aid. Hungary's financial difficulties, he thought, were not due to payment of reparations. Far more important were the wartime removals of property to that area of Germany which later became the American occupation zone.

Finland's turn to express her views on the peace treaty came on the same day as the encounter between Byrnes and Vyshinsky on reparations. The atmosphere was thus hardly favourable to a statement on this matter. Finland at the Paris peace conference found herself exposed to the cross-pressure generated by great-power disagreements.

Finland's views were given on 15th August by Foreign Minister Enckell, who proposed a reduction of the reparations sum from 300 million dollars to 200 million. Finnish reparations, which so far had been outside the disputes of the great powers, now became a bone of contention. Against the background of earlier discussion the reasons advanced by Finland for this reduction could not fail to cause annoyance to the Soviet delegation. According to Enckell's statement Finland did not expect to be able to improve her economic position by foreign trade alone. Without aid from abroad — Sweden and the United States — Finland would not have been able to maintain her modest living standard, reorganize

her production mechanism and pay reparations. Thus the idea was indirectly presented that Western help was of vital importance to Finland — more important, for instance, than goods received in trade exchanges with the Soviet Union.¹⁷⁷

From the Soviet standpoint the Rumanian speech had given a favourable picture of the reparations position, and Hungary had bypassed the matter by saying nothing about it. Finland's appeal was exceptional and provided new weapons in the disputes of the cold war. The Soviet reaction to Finland was sharply negative: the Finns, it seemed, had tried to gain Western support against the Soviet Union. There was in fact no question of this. The Finns felt their economic situation to be more difficult than a foreign observer might have realized. Also, for reasons of internal policy it was important for Finland's government to take the initiative as it had done, in order to avoid later charges of neglecting the opportunity. In addition Finland made a written proposal for the reduction of reparations to 200 million dollars. To support this request the Finnish delegation had prepared an explanation of the circumstances in which reparations were paid.¹⁷⁸

The Finnish proposal was novel in the sense that Rumania and Hungary had produced nothing similar. The Finns themselves did not see the matter in this light, but had in mind the discussions held in Moscow during spring 1946. They did not feel, moreover, that the Soviet Union had treated them with exceptional favour, at least with regard to reparations. The Soviet government wished reparations to be dealt with between the two countries, not brought into the international arena. Finland for her part made proposals only on her own account, and contact with representatives of other states was confined almost entirely to formal courtesy calls. Confidence was restored to Soviet-Finnish relations before the Paris conference was over, with the result that Finland was promised economic concessions. This meant in the first place that Finland was no longer obliged to pay fines for late deliveries of reparations.

177) Nineteenth Plenary Meeting, August 15, 1946, 4 P.M., FRUS 1946 III, pp. 236—240.

178) Observations on the Draft Peace Treaty with Finland submitted by the Finnish Delegation 26.8.1946, FRUS 1946 IV, pp. 282—297.

Paris: Economic Commissions

After discussion of the proposals made by former enemy countries the peace treaty drafts were submitted to sub-commissions to be put into shape. Reparation articles were dealt with in economic commissions, one for Italy, the other for Bulgaria, Rumania, Finland and Hungary. Australia, who actively tried at the peace conference to advance the interests of small and medium-size countries,¹⁷⁹ proposed changes in the reparation clauses of all five draft agreements. Those for Rumania and Finland were exactly the same, while for Bulgaria, Italy and Hungary it was noted that reparations were paid to more states. The proposal for change was first presented in the case of Rumania, for at the suggestion of the Soviet Union the economic commission for the Balkan countries and Finland began its work with the draft agreement for Rumania.¹⁸⁰

The Australian proposal had two main objectives. First, the claim of 300 million dollars was so large that reparations could bring the payer state to economic collapse or loss of independence. The burden imposed by reparations should therefore be lightened. Behind this view, undoubtedly, was the idea that the Soviet Union was trying through reparations to extract the maximum economic benefit from Germany's former allies and place them under its own supervision. Connected with this was a second Australian objective. Reparations should be removed from the exclusive surveillance of the Soviet Union. The proposal even went to the length of recommending that agreements between creditor and debtor be revoked and deliveries made on the basis of them should be reconsidered.

Australia proposed that these objectives be reached without, as yet, fixing the final sum of reparations. A special reparation and repayment commission would investigate the payment capacity of the country in question and propose a final sum within six months of the peace treaty coming into force. The commission would also

179) *The Smaller Powers and Germany*, *The Economist* 8.2.1947, pp. 228—229.

180) *First Meeting of the Economic Commission for the Balkans and Finland*, August 16, 1946, 4 P.M., FRUS 1946 III, pp. 246—247; *Second Meeting of the Economic Commission for the Balkans and Finland*, August 19, 1946, 4 P.M., FRUS 1946 III, p. 254.

fix a value for goods delivered to the Soviet Union since the armistice agreement and would deduct this from the total amount of compensation. The remainder would be spread over five to ten years with the following allowance made for payment capacity: the reparation sum would represent a certain proportion of the value of export and would be paid to the receiver state as a currency exchange transfer.¹⁸¹

This change proposed by Australia was opposed above all to Soviet interests, and Molotov's brusque response is thus understandable. But Australia was not supported by the Americans or British either. As Molotov pointed out, the Australian proposal, if approved, would probably have meant a delay of unspecified length in reaching agreement on reparations, because the final sum would be the object of endless dispute in the commission. It is noteworthy that the American representative Willard L. Thorp also rejected Australia's proposal on this ground. He thought it desirable for both parties to know the amount of the liability as soon as possible.

It was questionable whether a firm conclusion could be reached on a specific sum after six months' study. It was also pointed out that if the sum were left open the former enemy country would be obliged to sign a non-specific form of agreement. A clause similar to that contained in the armistice agreement was to be preferred for the further reason that the liability imposed on Rumania had not proved too heavy.

The above discussion was highly important in the matter of Rumanian, Finnish and Hungarian reparations. Britain and the United States did in fact approve the Soviet idea of mentioning a certain sum for reparations, which in autumn 1944 they had agreed with reservations to include in the armistice agreements. Experience had shown that the Soviet notion worked satisfactorily. In autumn 1946 the search for a solution of the German question was clearly following a different course from the Italian, Rumanian, Finnish and Hungarian cases, which could no longer be taken as precedents for Germany. On the other hand the problems connected with Germany suggested that if, as proposed

181) Amendments Proposed by the Delegation of Australia. Peace Treaty with Rumania, FRUS 1946 IV, pp. 674—675.

by the Soviet Union at Yalta, a fixed reparations programme had been defined — with reliefs added if necessary — many difficulties could have been avoided.

Australia's proposal was unsupported, and her delegation decided to withdraw it. This was the only initiative which led to important discussion in the economic commission while dealing with the reparations clause of the Romanian draft peace treaty. When the commission submitted a report on the results of its work it was possible to mention that representatives were unanimous in approving the clause in question.

For Rumania the United States considered reparations of 300 million dollars justified. For Hungary it proposed a reduction to 200 million. Of this sum the Soviet Union would receive 133 million while Yugoslavia and Czechoslovakia would share 67 million. The Americans explained their proposal by saying that Hungary's economy would not stand the original liability. The United States had made several moves for the solution of Hungary's economic problems, but without success so far. In comparing the payment capacity of Rumania and Hungary the Americans arrived at obligations which would be relatively the same for both countries if reparations for Hungary were reduced to 200 million dollars.

The Soviet Union tried to set aside the American initiative on technical grounds. At a plenary meeting of the peace conference on 15th August it had been agreed that all proposals for changes must be submitted by midnight on 20th August. Before this, observed Thorp, the United States had reserved the right to bring up the clause in question, and this had been done as soon as the turn of the Hungarian agreement arrived for treatment. The question of procedure was settled favourably for the United States, and it was decided to discuss the proposal.¹⁸²

The Soviet Union then sought to convince listeners that the imposed liability did not exceed the Hungarian capacity to pay. Payment of reparations had been eased by a two-year extension of the time limit. The country's industry had revived well, and there were good prospects for Hungarian economic development. The

182) Fortieth Meeting of the Economic Commission for the Balkans and Finland, October 2, 1946, 9 P.M., FRUS 1946 III, pp. 633—635.

Soviet Union emphasized that the new democratic Hungary admitted her obligation and on this basis wished to create more stable relations with other countries. The actual effect on Hungary's economic development would have been the return of Hungarian property from the American occupation zone of Germany. When a vote was taken, the American proposal did not receive sufficient support. Seven delegations opposed it, five supported it, two abstained from voting.¹⁸³

When Hungary's affairs had been dealt with, the draft for Finland was the next in line. On 4th October the United States submitted a proposal at a meeting of the Economic Commission for the reduction of Finnish reparations to 200 million dollars. As in the case of Hungary the United States made this proposal after the time limit was up. Because the Americans had not reserved the right to reintroduce the matter as they had done with the Hungarian draft, the chairman of the Commission did not allow the proposal on the agenda. The American representative Jacques Reinstein admittedly observed that procedure in this case was not the same as for Hungary because the American proposal supported observations made by the Finnish government. As the Americans could not change the clause they decided to vote against it. The same was done by the Union of South Africa, Canada and New Zealand. Nine delegations voted in favour, Australia abstained. As Australia had withdrawn her own amendment, article 22 on reparations was approved without changes by the Economic Commission.¹⁸⁴

After the case of Finland the Economic Commission examined the reparations liability of Bulgaria to Yugoslavia and Greece. In this connection Thorp mentioned that 300 million dollars imposed the smallest burden on Rumania, a heavier one on Hungary and a still heavier one on Finland. He was prepared, however, to take the Rumanian case as a starting-point for considering the others, and accordingly recommended the sum of 100 million dollars for

183) Forty-first Meeting of the Economic Commission for the Balkans and Finland, October 3, 1946, 10 A.M., FRUS 1946 III, pp. 636—638; Report of the Economic Commission for the Balkans and Finland on the Draft Peace Treaty with Hungary 11.10.1946, FRUS 1946 IV, pp. 535—566.

184) Report of the Economic Commission for the Balkans and Finland on the Draft Peace Treaty with Finland 8.10.1946, FRUS 1946 IV, pp. 573—589.

Bulgaria. After several votes had been taken the sum proposed by Britain for Bulgaria, 125 million, was decided on.¹⁸⁵

Paris: Plenary Meeting

No important changes were made by the Economic Commission in the reparations clauses of the draft peace treaties for the Balkans and Finland. When the drafts came up for reconsideration at a plenary meeting they had already taken shape. Despite this the American representative Senator Arthur Vandenberg proposed a further reduction in the reparations sum for Finland, but this did not have the result hoped for, Finland's liability remaining at 300 million dollars.¹⁸⁶

From spring 1944 onwards the United States had stood aside from the preparation of a peace treaty for Finland, basing its attitude on the fact that the countries had not been at war with each other. However, Washington regarded the reparations liability for Finland as reasonable. The Americans would not have granted credits to the Finns if they had doubted the latter's ability to pay reparations, and when the peace conference began, it was not mere concern with the Finnish situation which gave them a reason for proposing a reduction of reparations.

If the Americans had actually found the recent speech by Finland to be an important turning point, they had had several days in which to suggest changes.

In fact, American efforts to reduce Finland's liability were not based primarily on a wish to help the Finns. Finland was successfully meeting her obligation to the Soviet Union, and reduction of that obligation would have been a propaganda victory for the Americans. It could have been explained to the world that the sum demanded by the Soviet was too much. The American proposal did not question the main features of the provisions of the armistice agreement as the Australians had done, but was

185) Forty-fifth Meeting of the Economic Commission for the Balkans and Finland, October 4, 1946, 10 P.M., FRUS 1946 III, pp. 677—681.

186) Forty-sixth Plenary Meeting, October 14, 1946, 10 A.M., FRUS 1946 III, pp. 840—843; Forty-seventh Plenary Meeting, October 14, 1946, 3.30 P.M., FRUS 1946 III, pp. 843—856.

concerned only with the amount of the obligation imposed on the debtor. The Americans did not believe their proposal would go through, and it was therefore not important to ensure even that it came up for consideration. It was useful for Arthur Vandenberg to show concern in this matter: in his home state of Minnesota there was a substantial Finnish colony. The proposal had served its purpose when it had proved usable in the arguments of the cold war. The suggestion for a reduced sum of reparations was aimed more against the Soviet Union than in favour of Finland.¹⁸⁷

Paris: Italian Reparations

Proposals for changes in the draft peace treaty for Italy were first discussed in the Italian Economic Commission on 27th August. Before this Italy too had had the opportunity to express her views on the draft peace treaty. As the reparations clause — except for the Soviet share of 100 million dollars — was still open, the Italians did not comment on it apart from a few technical observations.

In the Italian case Australia had made substantially the same proposal for a change as in the previously mentioned cases. The reparations commission would have so directed payments to the Soviet Union and other Allies that within six months of the peace treaty coming into force the Italians would make currency transfers to the value of a certain proportion of their exports.

After the discussion on the Balkan countries and Finland these proposed amendments had no chance of approval. Despite this Australia did not withdraw them: her representative E. R. Walker defended his country's views. Australia did not wish to question reparations for the Soviet Union — it was merely that no one knew whether the sum in question was suitable. Once again Molotov strongly criticised the Australian proposal: Australia had proposed so many amendments that she must have had help in doing so. The Soviet proposal for 300 million dollars in all was a minimum claim for reparations which would not satisfy Yugoslavia and Albania at least. The Australian proposal for currency payments, on the other

187) Polvinen 1986, pp. 252—253.

hand, was clearly favourable to Western capitalists as it would force countries on the losing side to sell their goods cheaply to the West. In Molotov's opinion the settlement of reparations should not be delayed or left for "some superfluous commission" to examine.¹⁸⁸

Discussion of the proposed Australian amendment continued next day. After speeches by Greece and France Vyshinsky once more expressed Soviet criticism. And although South Africa was prepared to approve parts of the proposal, in the final vote it was supported only by Australia and New Zealand.¹⁸⁹

In a written statement the United States opposed the Australian proposal because in the opinion of the United States economic liabilities for states on the losing side should be fixed as soon as possible. For this reason a separate reparations commission was not needed, and payments as currency transfers meant troublesome credits from other countries.¹⁹⁰

On 30th August the Economic Commission for Italy decided to set up a sub-commission to consider reparations. Its members were Britain, the United States, the Soviet Union and France from the Council of Foreign Ministers and Yugoslavia, Greece and Ethiopia to represent the creditors. Czechoslovakia and Canada were also made members because they had made no claims on Italy.

Before the sub-commission began work the Economic Commission prepared to vote on the articles dealing with reparations for the Soviet Union. In this connection two important proposed amendments were presented. The first — once again from Australia — concerned itself with a commission to co-ordinate reparations deliveries. This was rejected, none of the great powers supporting it.¹⁹¹

The other proposed amendment was from Brazil, who believed that the article reading: "The USSR shall furnish to Italy on commercial terms materials..." ought to have read: "The USSR

188) Fourth Meeting of the Economic Commission for Italy, August 27, 1946, 4 P.M., FRUS 1946 III, pp. 293—294.

189) Fifth Meeting of the Economic Commission for Italy, August 28, 1946, 4 P.M., FRUS 1946 III, pp. 305—306.

190) Statement by the United States Delegation on Article 64 (s.d.), FRUS 1946 IV, p. 385.

191) Eight Meeting of the Economic Commission for Italy, September 2, 1946, 4 P.M., FRUS 1946 III.

shall, if necessary, furnish to Italy..." Brazil's reason was that the additional words emphasized that Italy could obtain raw materials from other sources and thus laid stress on freedom of trade. No wish to change the draft was evident: in the opinion of France the original text did not forbid Italy to obtain goods from elsewhere. Thorp, the American representative, emphasized for his part that the article obliged the Soviet Union to supply materials needed for current production deliveries without causing difficulties to the Italian balance of payments. In a written statement the United States pointed out that Italian reparations to the Soviet Union were of a special nature. The intention was that the Soviet Union should supply raw materials to Italy and that the Italian share should be "value added by manufacture." These supplies must not lessen Italy's opportunities to obtain foreign raw materials either for domestic consumption or to be used for the export industry, but the Soviet Union was also not prevented from obtaining these materials from other countries.¹⁹²

The Brazilian proposed amendment secured only four votes.

On the last day of August the Soviet Union had proposed to the Council of Foreign Ministers that an order should be added to the reparations article for pricing to be based on the gold parity of the dollar on 1st July 1946. When this was approved in the Economic Commission reparations to be received by the Soviet Union were settled.¹⁹³

The Economic Commission continued its work by hearing other creditors of Italy. The last speeches were made on 11th September, when Thorp spoke for the United States and Tarchiani for Italy.¹⁹⁴ Thorp stressed the magnanimity of his country, which had the right to claim compensation but had in fact given more than 100 million dollars in aid to the Italians. He admitted that "other nations which maintained large occupation forces in various countries might not be in the same financial position as the United States", so that some states could be considered entitled to partial

192) Statement by the United States Delegation on article 64 (s.d.); FRUS 1946 IV, pp. 385—386.

193) Ninth Meeting of the Economic Commission for Italy, September 3, 1946, 4 P.M., FRUS 1946 III, pp. 348—349.

194) Fourteenth Meeting of the Economic Commission for Italy, September 11, 1946, 4 P.M., FRUS 1946 III, pp. 425—427.

compensation.

Thorp did not neglect the opportunity to make propaganda for his country. As far the suspicion expressed by Britain and other Allies that the Italians were being let off too easily he replied that fascism and its consequences had laid a heavy burden on the country which should not be increased by excessive demands for reparations.

The Economic Commission now had to decide on the share of reparations for each creditor. In a voting process which lasted till early October this result was finally arrived at:¹⁹⁵

Albania	Nothing
Ethiopia	\$ 25 million
Greece	\$ 100 million
Yugoslavia	\$ 100 million
Total	\$ 225 million

The recommendations of the Economic Commission for Italy were discussed at a plenary meeting on 9th October. Reparations to the Soviet Union were decided unanimously. And although the shares to other states required a further vote, the amounts in dollars decided by the Commission remained in force.¹⁹⁶

195) Thirty-eight Meeting of the Economic Commission for Italy, October 4, 1946, 9.45 P.M., FRUS 1946 III, pp. 674—677.

196) Thirty-sixth Plenary Meeting, October 9, 1946, 9.30 P.M., FRUS 1946 III, pp. 727—758.

Germany Excluded from Agreements

Reparations from Germany?

Although preparation of a peace treaty with Germany was left till later, talk on the reparations which might be obtained from her continued during the autumn of 1946. After the thoughts expressed by Molotov in Paris General Sokolovsky, commander of the Soviet occupation zone — together with his subordinates — in summer 1946 brought up unofficially the possibility of increasing deliveries from current production as part of the German reparations programme. Capital transfers, on the other hand, might be broken off for as much as 10 years. The Americans, like the British, saw in the Soviet attitude an indication that transfers of equipment as booty and reparations had caused problems for the creditor, and the Soviet government was now merely trying in a new way to increase the material benefit obtainable from Germany.¹⁹⁷

In Paris Byrnes gave no indication whatever that Molotov's proposal might lead to a compromise which would settle the dispute over German reparations. The relevance of the proposal in that connection did not escape him, however. Besides a compromise the Soviet Union had other aims — so the Americans calculated. First, the Soviet Union was believed to be in a situation where its people wanted consumer goods so plentifully and quickly that the focus of reparations had to be shifted from capital goods to current production deliveries. The latter would secure for

197) Caffery from Paris to SD 24.8.1946, FRUS 1946 V, pp. 593—594.

the Soviet Union more goods than deliveries of equipment could produce at home, and in addition German industry would be firmly directed eastward. If, for instance, German industry exported 10 % of its output — as already in the Soviet zone — in the form of reparations to the Soviet Union, a stranglehold would be established in Germany such as the Soviet already possessed in Finland and the Balkans.

It should be especially noted that from the summer and autumn of 1946 onwards ever-widening political aims became linked with reparations in American thinking. When the war ended the United States worked for a settlement in which the occupation of Germany should be as short and cheap for the Americans as possible. Although the Soviet right to reparations was recognized it must not be realized at American expense. What preoccupied American decision-makers above all in the autumn of 1946 was whether through current production reparations the Soviet sphere of interest could be opened to a political system in the style of Western democracy. Finland and the Balkan countries who had paid reparations from current production provided an example which the Americans did not find at all encouraging.

After the current ten-year period the Soviet proposal also assured the Kremlin of an opportunity to decide whether equipment should be moved to its own territory or whether production in Germany would be more advantageous to the Soviet Union. Regarded as a whole, both politically and economically, the Soviet proposal appeared in American eyes a stronger effort than earlier to intervene in the management of German affairs. Solution of the deadlock was overshadowed by a strong suspicion of Soviet aims.¹⁹⁸

The alternative presented by the Soviet Union was not at once set aside by the Americans, however, although the British once again sharply rejected it. After talks with Byrnes and in conjunction with Control Commission work unofficial discussions were started by Clay and his economic adviser General (Brig. Gen.) Draper with Soviet representatives on the possibility of using German current production for reparations.¹⁹⁹

198) Durbrow from Moscow to SD 6.9.1946, FRUS 1946 V, pp. 602—603.

199) Clay to Echols 14.10.1946, Papers of General Lucius D. Clay I, pp. 269—270.

In public and in principle the United States did not rule out the possibility of an agreement over current production reparations, though in practice it was not believed to be possible. During a much publicized speech in Stuttgart on 6th September, for instance, Byrnes noted that reparations from current production were not mentioned in the Potsdam agreement at all, and that they were "incompatible" with the agreed production ceiling. Without mentioning Molotov's proposal he pointed out that the production level in question made a self-sufficient German economy possible, but no more. The United States had no wish to claim larger reparations from Germany than had been agreed at Potsdam. Byrnes made no comment on the idea that the production level might be raised and reparations equivalent to transfers of capital goods taken from current production — there was no agreement on the total sum of German reparations.²⁰⁰

A compromise on reparations might well have broken the deadlock on Germany. A settlement could have had still further advantages from the American standpoint. The decision to break off reparation removals meant also that the reception of reparations was deferred for other countries besides the Soviet Union. In IARA circles the United States was criticised more than before — there was even talk of the dissolution of IARA. The British and French were known to have used the occasion for explaining how the American decision punished receiving states unduly — the affluent Americans did not understand the problems of small European countries. Delay in settling the question of reparations caused problems in trade between European countries, and, in addition, when German factories stood idle their equipment deteriorated. Molotov's ideas were considered reasonable in Europe. But the American demand for Germany to be treated as an economic whole before any payment of reparations would have lost its credibility if the Americans had started deliveries to IARA countries alone — the German reparations problem had to be solved in its entirety.²⁰¹

At the negotiations in the Control Commission the Soviet Union outlined a proposal for reparations from current production which

200) See e.g. Ratchford & Ross 1947, pp. 242—251.

201) Acheson to Caffery in Paris 11.10.1946, FRUS 1946 V, pp. 611—613.

some Americans described as "reasonable". By its provisions the receiving state would supply the raw materials from which reparation goods would be manufactured in current production — as in the case of Italy the Soviet Union provided raw materials in this way. A central administration would be established for Germany including a department to supervise the implementation of a reparations programme from current production. The programme for transfers of capital would remain the responsibility of the zone commander — prohibition of transfers would be abolished — but otherwise economic boundaries between zones would be removed completely. For Germany as a whole an export-import programme would be drawn up. The Control Commission would agree on the amount of reparations from current production and at the same time revise the level of industry and plans affecting transfers of capital goods.

The Soviet proposal contained many demands made earlier by the Americans. The programme would have been based above all on the idea of treating all Germany as an economic unit. Still open was the question of occupation costs as well as the question of responsibility for the earlier deficit and that to be expected.

Reparation Terms

But concessions directly linked to reparations were not enough for the Americans. The objective was clear: "Undoubtedly at that time (= meeting of the Council of Foreign Ministers — HH) we shall want to tie in whatever agreement is made on this subject with political considerations. The Russian need for commodities out of German production is so urgent and apparent that we would be well-advised to use the opportunity to obtain very definite commitments from them on the subject of the introduction into the Soviet zone of occupation of our form of democratic methods."²⁰²

Proposed as a minimum condition for a reparations programme from current production was the establishment of rights of citizenship and political equality. "This may be our last opportunity to use such a potent bargaining position in Germany

202) Murphy from Berlin to SD 14.10.1946, FRUS 1946 V, pp. 621—623.

for this purpose."²⁰³

Among those who conducted foreign affairs for the United States were many who doubted whether concessions could be obtained from the Soviet Union in this connection. Messages from the American Embassy in Moscow suggested this in particular. Experience showed, it was stated, that the Kremlin was more willing to sacrifice economic aims than political ones.²⁰⁴

Those who supported trading thought that although there was nothing to gain, there was also nothing to lose. In the first place the "concessions" pursued by the Americans were, in their own opinion, merely a fulfilment of the Potsdam agreement — in other words the aim was merely to secure Soviet co-operation in something which they had in fact accepted. A reparations programme from current production might win Soviet assent to the above political conditions, but it was still possible for the Americans to cut off deliveries from current production. An agreement should not lead to a situation where the Americans would give up something without good reason while the other party could break the agreement with impunity. The United States owed its strong position mainly to its status as an occupier of Germany, where it could act effectively, whereas in the Balkans and in Finland the Americans had to be content with indirect means.²⁰⁵

The Soviet offer interested the Americans for the further reason that Germany's growing productive capacity would undoubtedly be an important factor in European reconstruction. If the Soviet Union supplied raw materials to Germany, the United States would not be obliged to give an enormous sum of dollars for German productive installations. Increasing production guaranteed employment, which in turn was expected to ensure social and political stabilization. The drawback was that increased production went at least partly to reparations, while with the aid of exports occupation costs could have been lowered immediately.

In Clay's opinion the advantages and drawbacks of reparations from current production were impossible to evaluate until a

203) Murphy from Berlin to SD 16.10.1946, FRUS 1946 V, pp. 623—625.

204) Durbrow from Moscow to SD 23.10.1946, FRUS 1946 V, pp. 626—629.

205) Murphy from Berlin to SD 25.10.1946, FRUS 1946 V, pp. 631—633.

comprehensive plan was made, based on dollar values and taking account of Germany's internal needs together with the export-import programme. Clay's view was that if the United States intended to agree to reparations from current production, no less than 11 preconditions must be met. They would guarantee fulfilment of most of the aims — political and economic — pursued by the Americans. On the economic side the resources of all Germany would have been used for both exports and reparations while an export-import programme and currency reform were carried out at the same time. In political matters freedom of movement, expression and association in the style of Western democracy would have been achieved.

Reparations from current production were the basic problem in Clay's opinion, and a solution must be found to it before disarmament and peace with Germany could be agreed. In the situation of that time the Americans had perhaps their last opportunity to break the supremacy which the Soviet was establishing over eastern Europe and East Germany.²⁰⁶

Moscow Conference of Foreign Ministers

Before reparations from current production were further considered by the foreign ministers an important change had occurred in the American political leadership. Secretary of State Byrnes had lost the President's confidence and planned to resign in the spring 1946. Having completed the preparation of peace treaties with the allies of Germany, Byrnes submitted his resignation. Appointed to succeed him in January 1947 was General George C. Marshall, who represented a firmer policy in relations with the Soviet Union.

When the Council of Foreign Ministers continued its work in Moscow during spring 1947 reparation claims for the great powers and the small IARA countries came up for discussion. Views on how to settle the question had been obtained from the countries of

206) Clay to Byrnes November 1946, Papers of General Lucius D. Clay I, pp. 279—284.

Europe.²⁰⁷ Among west European countries Greece and Norway in particular demanded substantial reparations, and so did Poland and Yugoslavia. As the Greeks saw it: "The amount of Germany's liability should be fixed at the highest possible level." This applied also to reparations from current production, and in addition technically trained personnel should be placed at the disposal of the Greeks as a form of compensation.

Belgium and Holland, on the other hand, were in favour of moderate reparations. It was necessary to wait until Germany was adequately self-sufficient and then consider the possibilities. At the same time while these states in some degree approved the reconstruction of Germany they expressed more often than before the notion of including her in a broader European economic system.²⁰⁸

At the conference of foreign ministers in Moscow the Soviet Union announced — as it had done earlier in the Control Commission — that it was prepared to approve Germany's being administered as a single economic unit provided that reparations from current production were first agreed on. The Soviet also re-emphasized its view that the German production level could be raised sufficiently to make reparations from current production a practical possibility.²⁰⁹

Discussion of reparations from current production began in Moscow with opening speeches by the foreign ministers. Bevin stressed the earlier standpoint of the Western Allies that an integrated economic administration for all Germany was an essential factor in the search for a settlement. In his opinion the German production level should be raised: important though it was to dismantle Germany's war potential, it was equally important to ensure that she was self-sufficient in peacetime. Bevin further stressed that the British could not approve any further burden of occupation, which meant in practice an unfavourable attitude to reparations from current production. His Majesty's Government was willing to work for the political and

207) Views of the Allied Governments on the Principal Aspects of the German Problem, FRUS 1947 II, pp. 85—89, 96—99.

208) The Smaller Powers and Germany, *The Economist* 8.2.1947, pp. 228—229.

209) Principal Economic Issues on Current German Problems for Council of Foreign Ministers' Meeting, Moscow, FRUS 1947 II, pp. 216—218.



General George C. Marshall, United State's Secretary of Defence and since January 1947 Secretary of State.

economic integration of Germany.

At the Paris conference Byrnes had announced that the United States was prepared to make agreements with each occupying power for the zones to be made into a single economic unit. After some uncertainty the British had assented, while the Soviet Union and France had declined. Earlier Molotov had strongly criticised the American and British agreement on the ground that it made possible the penetration of Germany by the economic empires of these countries. The Americans had replied to these charges by saying that American investment in Germany had not increased at all during the occupation.²¹⁰

Molotov continued the proposal he had made in Paris for a programme of reparations from current production, and appealed for fulfilment of the Yalta agreement. He was able to suggest plausibly that on the basis of this Soviet view the Allies might work together to revive Germany's peacetime economy, which

210) See e.g. Clay Contradicts Russia's Charges, The New York Times 1.3.1947, p. 5.

would enable war-ravaged countries to receive the goods they needed.

For his part Marshall asserted that Molotov's ideas contained no basis or logic for an Allied policy, and that charges and counter-charges in his opinion solved nothing. Like Bevin Marshall stressed again that to treat all Germany as a single economic unit was the key to solution of the problem.²¹¹

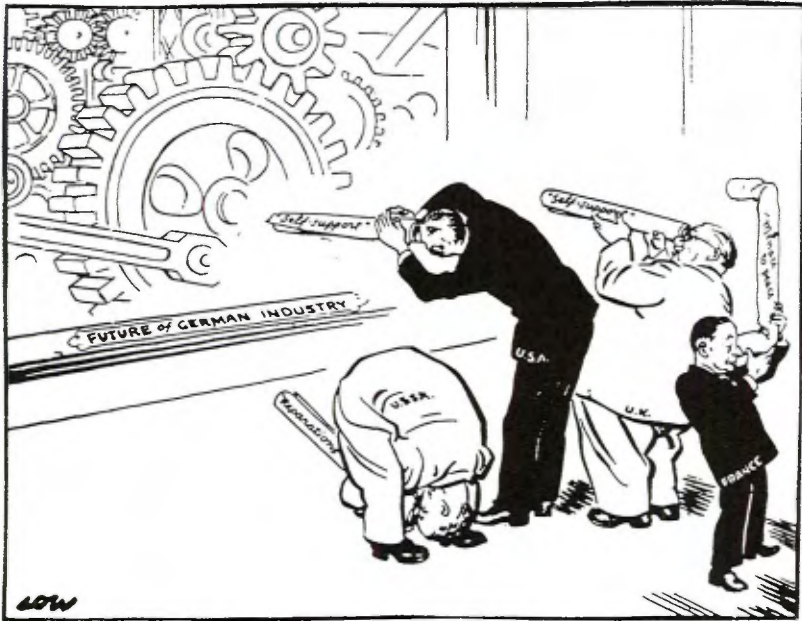
After the opening speeches the foreign ministers were obliged to decide whether a representative of IARA should be heard at the conference. Molotov and Bidault expected backing from this direction, for which reason they thought it was not right to bypass so many countries connected with the matter in hand. Marshall and Bevin thought, however, that an appearance by IARA was unnecessary. In their view all were agreed that a start should be made with reparations as soon as possible. There was disagreement on how obstacles to a solution should be removed, but an executive organization such as IARA could not help in this matter. It was finally agreed that the deputy foreign ministers should inform the Council of Ministers if IARA representatives had anything to add to the report they had submitted. IARA had no more influence than this on the negotiations of the four great powers.

The Soviet Union — whose reparation claim often featured in the west European press — wished to expose the fact through IARA that many other countries awaited reparations from Germany. Molotov branded the Western Allies as unwilling to dismantle the German war potential: in the Western zones, he stated, only three factories out of 1,557 marked for reparations had been dismantled to date. In the Soviet zone, on the other hand, 676 out of 735 had been stripped, Molotov exhorted the Western powers to consider without delay what factories should be sent to which countries.²¹²

According to Molotov American and British statements could give the erroneous impression that the Western Allies desired no reparations at all. Yet the Americans and British alike had received them from Germany substantially — gold and other German

211) Marshall to Truman 17.3.1947, FRUS 1947 II, pp. 255—257.

212) Molotov Demands Faster Disarming, *The New York Times* 12.3.1947, p. 2.



"The Big Four at Moscow as Mr. Low sees them" (The New York Times, March 30, 1940).

property, merchant shipping and German patents and inventions had been moved to the West. Relying on newspaper data Molotov placed their value at over 10 milliard dollars. In addition Great Britain, France and the United States were receiving reparations from current production, such as coal from the Ruhr and timber from south Germany.²¹³

Among the Western Allies Molotov's speech aroused violent annoyance, for they had been given a quite opposite picture of the situation. Bevin and Marshall challenged Molotov to reveal the information on reparations received by each country. A few days

213) United States Delegation Minutes 18.3.1947, FRUS 1947 II, pp. 257—262.

later American newspapers related that the United States had received various property from Germany to the value of less than 275 million dollars. German assets — depending on the method of calculation — amounted to 150—250 million, ships to five million, deliveries from IARA to 66 million and direct reparation deliveries to less than 10 million.²¹⁴

The Americans had published all patents and inventions which had come into their possession and sold them to all who wished to buy. A Soviet representative had been one of the most eager purchasers. Marshall called on the Soviet Union to do the same with the patents and inventions which had come into its hands.²¹⁵

The next object of dispute concerned what had actually been agreed regarding reparations. Even before the Moscow conference the Americans had given an interpretation of events by which the Potsdam agreement had superseded Yalta. Current production was not mentioned at Potsdam as a source of reparations, which meant — in the American interpretation — that the Allies had rejected this form of reparations altogether. The Americans announced that they would not follow the Soviets from Potsdam to Yalta.²¹⁶

In reality the Americans had not interpreted the Potsdam agreement in this way: in the Control Commission, for instance, they had negotiated on the possibility of putting into practice reparations from current production. Meeting Marshall at an unofficial discussion over lunch on 22nd March, Bevin too stated that Potsdam was not an indisputable replacement of the Yalta agreement though His Majesty's Government could not of course commit itself to such deliveries before the German economy was self-sufficient. According to Marshall those Americans in particular who had been both at Yalta and at Potsdam were convinced that their own interpretation was justified.

In Marshall's opinion the Soviet attitude could be understood simply thus: removals of capital goods had not benefited creditors sufficiently and the effort was being made to gain more advantage through current production deliveries. But there was no need to

214) Reparations Paid to U.S. Disclosed, *The New York Times* 26.3.1947, p. 3.

215) United States Delegation Minutes 18.3.1947, FRUS 1947 II, pp. 257—262.

216) Marshall to Truman 18.3.1947, FRUS 1947 II, pp. 262—263. Marshall Disputes Soviets, Rejects Reparations Bid, *The New York Times* 19.3.1947, p. 1.

give the Soviet government a means of influencing economic matters in the zones occupied by the Western Allies.

The American press repeated the views of its political leaders to the world. Marshall's warnings against allowing German industrial reconstruction in the guise of reparations were presented as eagerly as the claim that the German economy at that time could not sustain reparations from current production combined with the requirements of occupation forces and the Germans themselves.²¹⁷

Molotov stated that the Soviet Union took the regulations of the Potsdam agreement as its main starting-point — the unwillingness of the Western Allies to act on its reparations articles had led to a deadlock. The Yalta and Potsdam agreements complemented each other in his opinion, nor did Potsdam forbid compensation from current production by any means. In the Soviet view the opening phrase of the Potsdam agreement: "In accordance with the Crimea decision" indicated that the Yalta agreement had not been changed at Potsdam.

The obligatory nature of these agreements was ultimately of secondary importance to the great powers — the political content was the important aspect. In his above-mentioned meeting with Bevin Marshall did not place himself in complete opposition to reparations from current production. In accordance with discussions at the Control Commission he said that the United States was considering the possibility of bringing raw materials from the Soviet zone for manufacture in Western zones. It must then be ensured, however, that the development of a self-sufficient German economy was not delayed. Marshall thought nevertheless that it was almost impossible to guarantee Congressional approval of a settlement which included reparations even indirectly. On these grounds Marshall felt that reparations from current production could not be thought of as a practical possibility for at least the next two years.

Bevin promised on his own account to consider arrangements in

217) See e.g. U.S. is Urged to Stress Potsdam Formula on Reparations at Moscow Conference, *The New York Times* 10.3.1947, p. 4; Marshall Warns against a Revival of German Power, *The New York Times* 20.3.1947, p. 1; Warning on Reparations, *The New York Times* 22.3.1947, p. 1; Soviet Plan Held Peril to Germany, *The New York Times* 31.3.1947, pp. 1—3.

accordance with the above, but next day he sent a letter stating: "His Majesty's Government would not find it possible to agree to any settlement of the German problem involving reparation from current production which would entail further expenditure by His Majesty's Government."²¹⁸

In Moscow the great powers came up against several conflicts which had arisen over settlement of the German question. In Clay's opinion the basic issue for the Council of Foreign Ministers was not Germany's demilitarization, denazification or democratization; it did not consist of population transfers any more than of territorial dispositions. The central questions for the conference were problems of the economy and reparations. Although the Soviet proposal for reparations from current production was not acceptable without preconditions, it was worth while — if an agreement of the great powers was desired at all — at least to elucidate what was required for reparations from current production.²¹⁹

From Moscow on the last day on March Marshall sent Truman a report stating that negotiations on the level of industry and on reparations from current production had reached a decisive stage. Marshall thought that in principle it was possible to increase German peacetime industry on the basis of four-power agreement. It would require factory installations which had been primarily marked for reparations. Marshall suggested to Truman that he be given authority to examine the possibilities for reparations from current production up to the value represented by the above installations if they remained outside reparations. Also, the amount of reparations from current production would depend on Germany's ability to increase the export surplus. In no case would such a plan be carried out before the economic and political integration of Germany was an accomplished fact.²²⁰

At a meeting of foreign ministers held on 31st March all the parties concerned repeated their former standpoint. Marshall

218) Memorandum of Conversation (Marshall) 22.3.1947, FRUS 1947 II, pp. 273—275.

219) Clay's Memorandum 30.3.1947, Papers of General Lucius D. Clay I, pp. 328—331.

220) Marshall to Truman 31.3.1947, FRUS 1947 II, pp. 298—299. Paterson 1975, pp. 244—245.

pointed out that although the foreign ministers in Moscow were resolving their differences, they should not seek an agreement merely for its own sake. The Americans admitted, he said, that their responsibility in Europe continued, and they wished to build solidly rather than quickly. For his part Bidault still linked the matter of German coal and the Saar territory with reparations, while Bevin saw no chance of reparations for the next few years. Molotov still insisted on a reparations agreement in concrete terms which would include raising the German production level and increasing exports and imports.²²¹

In the absence of new instructions from Washington Marshall presented the above ideas at the following day's meeting. Without committing themselves to anything as yet, the Americans were willing to examine the possibilities of reparations from current production in a situation where these reparations would compensate for the ending of removals of capital goods as Germany's production level rose. It should be remembered, of course, that the British opposed all reparations from current production.

Molotov could not accept the American offer. Reparations from current production could not compensate for the cessation of removals of capital goods. Raising the production level did not lead to a reduction in the number of factories marked for reparations, but raising the level made reparations from current production possible. Views on Germany's possibilities for paying reparations differed greatly.²²²

But the innermost conflict was not concerned with the amount or nature of reparations in themselves. The examples of Rumania, Hungary and Finland had shown the Soviet Union how beneficial reparations from current production were. For this reason the Soviet government demanded logically that agreement should first be reached on the principle of reparations from current production; it was only then that the foundations would have been laid for practical realization. The Western Allies, on the other hand, demanded the integration of Germany first: only after this — if the German economy stood the strain — could reparations be discharged from current production. In public the Americans were

221) Marshall to Acheson 31.3.1947, FRUS 1947 II, pp. 299—301.

222) Marshall to Acheson 1.4.1947, FRUS 1947 II, pp. 303—304.

able to show the Soviet Union and its partial supporter France in a doubtful light: by demanding both a higher production level and reparations from current production these countries were about to repeat the mistakes following the First World War in building up German strength with the support of reparations. "We must avoid at all cost establishing conditions in Germany similar to those after the First World War, when in an incredibly short period of time Germany, through increased production for reparations and foreign loans, was able to build up her internal economy geared for war."

Less attention was attracted by a later point in Marshall's statement : "At the same time under no conditions should we set her (= Germany — HH) so low that a democratic life could not hope to survive in Germany."²²³ The basic motive of American policy was not fear of German military growth. If it had been, the Americans would not have planned the programme of reconstruction which became known as the Marshall Plan. Just as no agreement was made with the Soviet Union for reparations from current production, so the Soviet government was provided with no means of influencing the management of economic affairs outside its own zone.

The Moscow conference had reached a deadlock which the foreign ministers could not break. As the conference gave rise to nothing more than charges and counter-charges Clay asked permission on 31st March to return to Germany²²⁴ A few days later Clay instructed his subordinates that he was prepared to consider a new production level only on the basis of the American and British zones. To the Soviet Union and countries under its supervision reparations could not be delivered, and this also made the work of IARA impossible.²²⁵

One consequence of the Moscow conference of foreign ministers was that the great powers found no solution to the question of German reparations. The Western powers estimated that during the 1950s Germany might reach a level at which an export surplus

223) Marshall to Truman 19.3.1947, FRUS 1947 II, pp. 263—265. Marshall Warns against a Revival of German Power, *The New York Times* 22.3.1947, p. 1. Warning on Reparations, *The New York Times* 22.3.1947, p. 12.

224) Clay to Marshall 31.3.1947, Papers of General Lucius D. Clay I, p. 332.

225) Clay to Draper 2.4.1947, Papers of General Lucius D. Clay I, pp. 332—333.

could be achieved. Repayment of loans taken out in previous years would take 10—15 years, so that during the 1960s it might be possible to return to the question of reparations from current production. Sympathy for the Soviet Union was certainly felt in Europe: when the reparations programme came to nothing the Soviet were in fact obliged to sacrifice the goods they were to receive from Germany — which were, they thought, the least of their entitlement.²²⁶ But the unyielding attitudes adopted by the parties concerned produced a situation which did not even allow discussion of the substance of possible reparations.

The Soviet Union had decided to obtain immediate satisfaction from Germany and Eastern Europe. The Americans and British were equally determined to secure the economy of a self-sufficient Germany which would in turn help the whole of Europe onto its feet. Deadlock between the great powers seemed almost unavoidable. It could only have been avoided by finding such concessions as were worth making for the parties concerned. The Soviet Union might have dispensed with reparations from current production if it had obtained the equal benefit of a loan from the United States. The United States held the key position in seeking a solution, but did not wish to give a dollar loan to the Soviet Union. To the Americans the policy of the Soviet Union appeared to be the creation of a self-sufficient, closed and powerful bloc as opposed to creating fruitful contacts through an open door policy, and so the dollars remained on the other side of the Atlantic.²²⁷

As the war ended it was undoubtedly expected in the Soviet Union that substantial material assistance would be received from the West to repair the damage of war. Reparations were one method, but wartime aid was expected to continue in peacetime. During the war the Americans and British had understandably gained the reputation of friends of the Soviet Union, and this could not easily be changed in public opinion. Germany's future constitution — whether based on a central administration or a federation — was a distant matter to most of the Soviet people. But during the Moscow conference, when the course of negotiation was widely followed in the Soviet Union, Molotov was able to

226) Moscow: Reparations Deadlock, *The Economist* 29.3.1947, p. 448.

227) Failure of a Mission?, *The Economist* 12.4.1947, pp. 521—522.

appeal effectively to his fellow-citizens by "revealing" that Bevin and Marshall had ruined the Soviet reparations plan.

The Soviet people were told of the Yalta and Potsdam agreements, of Soviet willingness to increase the extent of the German steel industry, and of other concessions so that reparations might be carried out. When Western leaders appealed to the heavy burden on American and British taxpayers there was certainly no response among Soviet citizens. Even if the Western powers were obliged to feed the Germans for some time, the expense entailed was not to be compared with the destruction caused to the Soviet Union. Why was the feeding of Germans in the forefront of speeches by Western leaders while nothing was said of helping the Soviet Union? Also, the Western powers appeared as breakers of the Yalta and Potsdam agreements: this was how Anglo-Saxon gentlemen honoured their commitments and promises.

After the war there was much talk in Western circles of how Soviet diplomacy squandered the goodwill which the Soviet Union had gained in the West during the war. By the spring of 1947 it appeared that the same had happened in the opposite direction. Marshall and Bevin wasted the moral trust in Western democracy which had sprung up among the Soviet people and which was evidently greater than the West knew. By refusing to approve reparations from current production the Western leaders had given the Soviet leaders a form of moral reparation on whose basis the latter could justify their own policy.²²⁸

228) Reparations and the Russian People, *The Economist* 12.4.1947, pp. 542—543.

Conclusion

With regard to all the European countries on the losing side except Germany herself the Allies reached agreement on reparations. Germany's position amid the powerful conflicting pressures of Eastern and Western interests was such that no solution for her could be found.

When a reparations settlement was planned during the war the Americans understood Soviet aims to a great extent and were prepared for concessions, while the British opposed any Germany the situation changed. Soon after the war ended it became evident that for the reconstruction of Germany loans were needed. The British were especially conscious of the dangers connected with occupation of a country which was economically weak. In autumn 1945 the situation already looked chaotic: food supplies grew steadily worse, and, as a further example, in the iron industry of the Ruhr output was about 1 % of what it had been a year earlier. The Economist noted that "to compress fifty to sixty million people into a territory roughly the size of Britain and then totally de-industrialise it can only lead to the collapse and the disaster we are already witnessing."²²⁹ The British understood Soviet claims for reparations — no one thought them unreasonable in relation to the destruction the country had suffered — but the Germans immediately after the war were in no position to pay.

When the war ended it was clear that the revival of Germany required external economic help in some form or other. In practice only the United States could give such help — Britain's own economy was badly in need of dollar credits. In a political sense to give loans — American taxpayers' dollars — to a country which had been an enemy a few months before was a doubtful procedure

229) A Policy for the Ruhr, *The Economist* 8.9.1945, pp. 321—322.

for the country's leaders. The struggle between democracy and dictatorship was stronger in the popular mind than a confrontation of the socialist and capitalist systems.

As an alternative to loans the political leaders of the United States and Britain often expressed the notion that the integration of Germany would have made German revival possible. Predominantly agricultural eastern Germany would have fed the western parts, and the industrial surplus of the west would have paid for essential imports. The conditions imposed by the Soviet Union and France, however, brought the American and British plans to nought.

In any case such ideas would have had little chance of realization in postwar Germany. Economic problems in all zones were so great that without external help there was no solution. The transfer of Germany's eastern territories to Poland and the reparations taken by the Soviet Union from its zone affected the general situation only a little, however. Reconstruction in both the Soviet and French zones would have had to be financed by the Americans, and in addition a fusion of the American and British zones was already costing a great deal. But it is obvious that the integration of Germany would not have been as straightforward a solution, economically, as the American and British attitudes suggested.

The economic problems would have been best solved, undoubtedly, by an expansion of German industry. An export surplus would then have begun to accumulate, enabling the Germans both to repay loans and discharge reparations. Such had happened in the case of Finland.

Charles P. Kindleberger has estimated with good reason that Finland's success in discharging the heavy liability imposed on her was due to a favourable current account in foreign trade, to foreign loans and to the relief granted by the Soviet Union the matter of reparation obligations. But the main factor was the Finnish resolve to carry out the reparations programme. "Indeed it can be argued that the foreign credits and the Soviet concessions were the consequences of that resolve, and that the help of favourable terms of trade was altogether secondary."²³⁰

230) Kindleberger 1986/1987.

The case of Finland showed that even a heavy reparations programme could have been carried out if the great powers had agreed on the political preconditions. The reparations settlement of Versailles had taught the Americans to be cautious in granting loans to countries paying reparations. Immediately after the Second World War loans were granted to Germany only to save the country from a financial crisis. But the object of postwar loans was supposed to be the revival of production. After this was achieved Germany would have had a chance of self-sufficiency — provided that an expedient policy was followed in other respects. As an economic problem German reparations were not especially difficult — their payment would have been possible as a by-product of reconstruction. But for political reasons to give a loan, whether to the enemy of previous years or to an ally as a reparation, was impossible for American leaders.

By the time of the Potsdam conference differences between the great powers on reparations were not yet too great to be overcome. Reparations on a zonal basis reinforced the division of Germany, and the solution proposed by the Americans meant in practice a change in the realization of their aim to include all Germany in a single economic unit. At Potsdam the Allies had only Hitler's mistakes to correct — in spring 1947 the foreign ministers also had their own. The reparations settled in the armistice agreements were brought into final peace treaties, but the question of German reparations remained completely unsettled.

Despite differences over matters of detail the Americans and British wanted the same things. Germany, they thought, should be reintegrated and the occupation troops brought home as soon as possible. To continue the division of the country was politically unwise, because German efforts for integration might reanimate national feeling. To avoid providing for others the Americans and British wished to make the Germans self-sufficient as soon as possible; it was believed in addition that a reviving country would be a poor basis for extremist movements, whether right- or left-wing. As time advanced following the end of the war the belief began to emerge that the revival of Germany and Europe was impossible without direct American aid.

The primary Soviet objective was to obtain satisfaction for the destruction it had suffered. At Potsdam the Soviet Union was prepared to reduce its claim substantially, an indication that in

return for a large dollar loan it might have waived its claim altogether or lowered it to a merely token level. Yet the Potsdam agreement signified that the collection of reparations was a settled matter, and the Soviet Union in its own zone began to act accordingly. Reparations from the Western zones remained on a small scale, however, which — as the Soviet Union rightly pointed out — deterred the Americans and British from carrying out the agreed programme in its entirety. To the Soviet Union integrated rule for all Germany and reparations from current production were undoubtedly tempting for the added reason that through them it might extend its influence to the economic life of the Western zones of Germany.

The Americans would have been placed at an economic disadvantage by the integration of Germany — especially after the Soviet Union had removed a substantial part of the equipment from its zone — whereas the Soviet Union would have safeguarded not only the capital transfers it had already obtained but also reparations from current production and would have obtained at least the indirect possibility of influencing the economic life of Germany. For the Americans and British the integration of Germany had become a political symbol, and to achieve it they were prepared to make economic sacrifices — if the Soviet Union and France had agreed to the political conditions involved. By the time of the Moscow foreign ministers' conference the question was in essence whether the Soviet Union would bow to these conditions imposed by the West.

If the choice was between German integration with reparations on Soviet terms and no integration or reparations, there was widespread willingness in the Western world to give up both. To be sure, integration was hoped for by many, but the pressure in that direction, it was believed, would in any case gradually increase till in due course it was irresistible. On the other hand a reparations claim, once approved, might poison European diplomacy for generations, as had happened after the First World War.

At the same time as reparations were appearing less desirable to the Western states for a number of reasons, no alternative to them had become visible to the Soviet Union. Soon after the war American dollars were available for the British, but not for the Soviet Union. As aid for Germany was discussed more openly in

the West, forecasts of a capitalist world united against socialism seemed to be coming true. The foreign ministers' conference in Moscow would certainly have had a different atmosphere if Washington had acceded even in part to the Soviet request for a loan.

The political conditions for a loan naturally could not have omitted the central interests of the Soviet Union, but the great powers in the end made no attempt to seek a compromise in this matter. A loan might well have removed reparations as a conflict between the great powers, and if the Soviet Union had been admitted to the supervision of the Ruhr an economic solution satisfactory to all parties evidently might have been found. Even in January 1947 *The Economist* estimated that a more broadly favourable solution would be reached in this way.²³¹

During the war the Allies adopted the idea — without actually discussing other alternatives — of strict supervision for Germany when hostilities were over. In this respect events following the First World War caused no misgivings — matters had merely been conducted wrongly in practice at that time. During the war it had been taken almost for granted by all that when peace returned Germany would have to submit to disarmament and other restrictions.

When the war ended, on the other hand, several alternatives emerged to the policy then being operated by the great powers. *The Economist*, for instance suggested in several articles the idea of a punitive period for Germany, to last only for a year or two once peace returned. During this period war criminals would be tried and reparations paid but once it was over the Germans would gain full sovereignty — except in respect of disarmament, which the Allies would still be obliged to supervise. Reconstruction of the dismantled armament industry would be prevented by forbidding the inclusion of commodities intended for this purpose in Germany's foreign trade. The main starting-point of the plan differed, however, from the policy actually adopted by the Allies: it rejected plans for limiting German economic growth, and peacetime industry was to be allowed to grow.²³²

231) German Unity in Question, *The Economist* 18.1.1947, pp. 91—92.

232) See e.g. Is a German Compromise Possible?, *The Economist* 20.7.1946, pp. 83—84.

The question of German reparations was a political problem in great-power relations at a time when many factors were leading to conflict between East and West. After a common Allied decision had been reached over reparations for Italy, Rumania, Hungary, Finland and Bulgaria, relations between the great powers were not noticeably strained by putting reparations into effect. With regard to Germany the great powers came near a solution which, if realized, might well have turned the course of events in quite another direction.

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Abbreviations

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Cab	Cabinet Office
FO	Foreign Office
FRUS	Foreign Relations of the United States
NA	National Archives, Washington D.C.
Prem	Prime Minister's Office
PRO	Public Record Office, London
RG	Record Group
VA	Valtionarkisto, Helsinki

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