BREXiT UNIT

Should the UK pay an EU divorce bill?

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The Brexit negotiations will need to decide how much the UK will pay the EU to settle financial obligations undertaken while it was a member. Some EU officials have suggested that the bill should be €100bn. Many Brits would counter that the right figure is 'zero'.

A compromise might be acceptable provided the UK gets something in return. A maximum figure of around €30bn (£26bn) could be justified based on obligations until 2020. But if the two sides fail to agree a good deal on their future relationship, including any transitional arrangements, the UK can, and should, walk away without paying a penny.

Divorcing, or quitting a club?

Stepping back a bit, the term 'divorce bill' is actually a little misleading. The EU existed before the UK joined and will (probably) last long after the UK has left. It is not therefore a simple matter of dividing up assets and liabilities in the same way as a divorcing couple might sell the family home or fight over custody of the dog.

A better analogy is leaving a club. The UK agreed to pay membership fees in return for access to the facilities and services provided by the EU and now needs to close its account. What's more, these should be sums that the UK would have had to pay anyway even if it remained a member. As such, the exit bill would not be an additional 'cost' of leaving (as many Remainers like to claim).

UK is on strong legal ground, but should be flexible

This still begs the questions of why the UK's contributions should not simply cease in March 2019 and, especially, why the UK should continue to pay towards EU spending that will take place after the UK's departure. Indeed, the House of Lords has concluded that, on the basis of Article 50, the UK would be on strong legal ground if it declined to pay any divorce bill at all.

But this approach may backfire. A more flexible stance should increase the chances of getting better terms on other aspects of the negotiations which will ultimately be more important – including a bespoke free trade deal. Rather than sticking to the letter of the law, the UK could earn some goodwill (and tangible benefits) by focusing on the spirit of the past and future relationship.

Key Points:

- The UK is leaving the EU and needs to close its accounts.
- In a divorce, the two sides divide up the assets and liabilities. But the situation here is more like leaving a club, so the question is when the obligation to pay membership fees should end.
- One option would simply be for the UK to cease payments at the end of March 2019 (with no bills thereafter). The UK would be on strong legal ground if it decided to do so. Article 50 is clear that, in the absence of any other agreement, EU Treaty obligations will cease to apply after that date.
- However, a more flexible stance could help secure better terms on other aspects of the negotiations, including any transitional arrangements before a comprehensive free trade deal can be concluded.

A cut-off date of 2020 would be fair and reasonable

In particular, the EU made long-term financial commitments during the period of the UK's membership, (mostly) agreed by the UK, and on the assumption that the UK would continue to contribute. Given this, there is a decent case for arguing that the UK should make its usual payments until the end of the EU's current Multiannual Financial Framework (MFF), which runs from 2014 to 2020.

This is similar in principle to quitting a club: if you have signed up to a long-term subscription you might still be liable for the whole amount even if you decide to leave early.

My back-of-the-envelope calculations suggest this would imply a divorce bill of no more than €25bn (net of the UK's rebate and EU spending in the UK), to cover the period from March 2019 to the end of 2020.

I would add a few smaller one-off items, notably a contribution to pension payments for EU officials, which would take the total bill to around €30bn (approximately £26bn).

This would be equivalent to significantly less than three years of the UK's current annual contributions – arguably a small price to pay to secure a better relationship with substantial advantages long into the future. Depending on how the negotiations play out, it could also cover an interim period after March 2019 when the UK is benefiting from any transitional arrangements.

- It seems fair that the UK should be asked to make some contribution towards long-term financial commitments undertaken when the UK was a member – even if the money is spent after the UK has left.
- A sensible cut-off date would be the end of 2020, when the EU's current multi-year budget process is completed.
- If the UK continues its planned payments until then, the bill would come to around €25bn, which might be topped up to €30bn (£26bn) with a few reasonable extras.
- However, the EU is demanding a lot more than this, including large contributions to spending likely to take place long after 2020, and upfront payments for contingencies that may never materialise.
- If the EU is unwilling to compromise, the UK can, and should, walk away without paying a penny.

But the EU is padding the bill

However, the EU is asking the UK for a lot more, including large contributions to spending which could take place long after 2020. The calculations here become hugely complicated, but the Bruegel think tank has made heroic efforts and the FT's Alex Barker is good on the politics.

In a nutshell, EU officials have demanded that the UK contribute its full share of the following: current spending up until at least 2020, including on the Common Agricultural Policy and EU running costs; long-term capital spending, including structural funds; and money allocated in current and past MFFs that has not yet been paid out (known by the French 'Reste à Liquider'). There is some overlap between these categories, but the key point is that the UK's usual annual payments would not be enough to cover all of them.

Frankly, this is going too far. The EU needs to adjust its spending to reflect the fact that one of its biggest net contributors is leaving. A grace period until the end of 2020 would surely be long enough.

The EU is also asking the UK to make large upfront payments for contingencies that may never arise – and then wait years for a repayment. The main item here is guarantees on loans made by the European Investment Bank. It would make more sense to amend the paperwork so that the UK can remain a counterparty on the current terms, rather than require large payments back and forth.

Split the difference?

Altogether, the EU's demands add up to a gross bill of around €100bn. And on this basis, the net bill would still be at least €60bn, and probably much more, even after allowing for the UK's rebate (itself in doubt), EU spending in the UK, and future refunds on contingency payments.

Fortunately, these are early days in the negotiations and there is surely room for compromise. As it happens, the figure of €30bn suggested above would be consistent with meeting half way between the EU's net €60bn and the UK's fall-back position of zero. But if there is 'no deal' by March 2019, the UK should be ready to start saving money straightaway.

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