HOUSE OF COMMONS LIBRARY

BRIEFING PAPER

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The UK's contribution to the EU Budget

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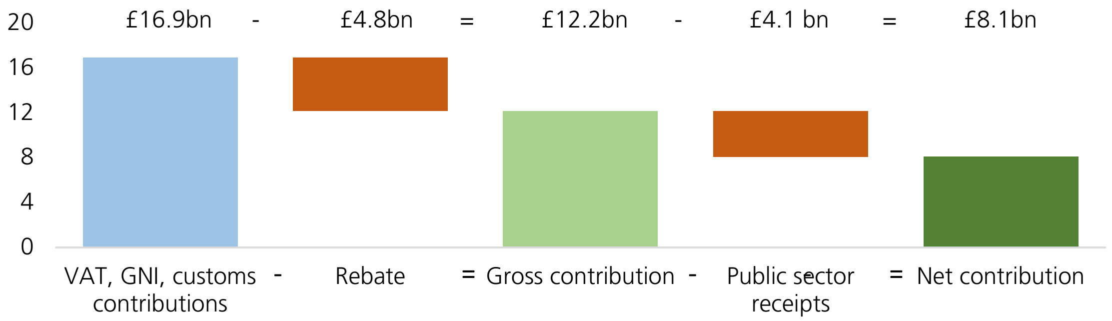
The UK's contribution to the EU budget

As a member of the European Union the UK makes payments, or contributions, to the EU budget. The UK also receives funding, or receipts, from the EU. The EU provides funding for various agricultural, social, economic development and competitiveness programmes.

The UK receives a rebate from the EU which reduces its contribution. The rebate aims to correct the issue of the UK making relatively large net contributions to the EU.

In 2016/17 the UK made an estimated gross contribution (after the rebate) of £12.2 billion. The UK received £4.1 billion of public sector receipts from the EU, so the UK's net public sector contribution to the EU was an estimated £8.1 billion.

UK's contribution to the EU budget, 2016/17, £ billion



There are different ways to measure the funds the UK receives from the EU. The above figure of £4.1 billion includes only funding allocated to the UK government to manage. However, the European Commission also allocates funding directly to UK organisations, often following a competitive process. In recent years these funds have been worth around £1 billion - £1.5 billion to the UK. Accounting for these receipts results in the UK making an average net contribution of £7.1 billion between 2010 and 2014.

Brexit and the UK's contribution

The UK will remain a member of the EU until its departure has been negotiated and will continue to contribute to the EU budget until it formally leaves.

A payment on leaving?

The EU expects a payment from the UK to cover its share of the EU's outstanding spending commitments and liabilities when it leaves. This has been described in the media as an 'exit bill' or 'divorce bill'; the EU see it as settling the accounts. The payment is being negotiated as the 'single financial settlement' in the first phase of Brexit negotiations.

Estimates of the net payment range from less than €10 billion to €75 billion. The estimates vary based on the items included and how these are shared. The UK Government says it will meet its obligations, but reject speculation of a large settlement.

Payments after leaving?

In February 2017 the Government's Brexit White Paper said that the UK may pay to participate in some EU programmes after Brexit. For instance, the UK might pay to remain in Horizon 2020, the EU's research and innovation programme. Exit negotiations will determine the extent of the UK's future participation in EU programmes and any cost.

This briefing focuses on the UK's involvement with the EU budget. The Library briefing *A guide to the EU budget* discusses how the EU raises and spends money.

1. The UK and the EU budget

1.1 Introduction

As a Member State the UK makes payments, or contributions, to the EU budget. The EU also spends money in the UK, through various funding programmes. The EU's spending programmes include funds that support agriculture, develop regional economies and improve competitiveness.

The majority of the EU's spending in the UK is for agriculture and economic development.

Like all Member States, the UK contributes to the EU budget through three sources:

- it collects customs tariffs and levies on behalf of the EU. 20% of the tariffs collected are kept by Member States to cover the cost of collection.
- it contributes a percentage of its adjusted, or harmonised, VAT-base.
- it contributes a percentage of its Gross National Income (GNI).

The UK receives a rebate on its net contribution. The rebate was introduced in 1985 to correct the issue of the UK making relatively large contributions to the EU budget while receiving relatively little receipts from it. The rebate is deducted from the UK's contributions before it makes its payments to the EU budget.

The UK contributes to the EU budget in the same way as other Member States, but receives a rebate on its contribution.

There is more on EU spending, revenue raising and budget processes in the Library briefing *A guide to the EU budget*.

Box 1: Brexit and the UK's contributions to the EU budget

On 23 June 2016 the UK voted to leave the EU. The UK will remain a member of the EU until its departure has been negotiated and will continue to contribute to the EU budget until it formally leaves.

Once the UK has left it may still make payments to the EU. Exit negotiations will determine whether the UK makes any payments to the EU on leaving or after it has left. Section 3 of this briefing discusses the issue in further detail.

A payment on leaving?

The EU expects the UK to make a payment when it leaves the EU – this has been referred to as a 'divorce bill' or 'exit bill'; the EU see it as settling the accounts. The payment is in respect of the UK's share of outstanding EU commitments and liabilities. The size of any potential payment is very difficult to estimate and will ultimately be determined in the first phase of Brexit negotiations, where it is being discussed as the 'single financial settlement'. Which commitments, liabilities, and assets, are to be shared, and how they are shared, will form part of negotiations.

Contributions after leaving?

Following a negotiated departure, the UK may continue to make contributions to the EU budget. Any future contributions will depend on the formal relationship the UK has with the EU once it has left. It is possible that the UK may continue to participate in some of the EU's programmes, and would make financial contributions to do so. Prime Minister Theresa May – in a speech setting out the UK's objectives for exiting the EU – said that the UK may continue to participate in some EU programmes.[1]

Again it is difficult to estimate any future payments. It is fair to say that the greater the UK's access to EU programmes and the single market, the larger its ongoing payments will be.

[1] 10 Downing Street, The government's negotiating objectives for exiting the EU: PM speech, 17 January 2017

1.2 UK contributions and receipts

Different approaches are used for measuring the UK's net contribution to the EU budget. This briefing largely discusses HM Treasury's approach, but figures from the European Commission are provided in Box 3. The key difference between the sources is that HM Treasury include only EU receipts allocated to the UK government to manage, described as public sector receipts. Funds allocated directly to UK organisations by the Commission are not included by HM Treasury.

Gross contribution

HM Treasury estimate that in 2016/17 the UK made a gross contribution of £12.2 billion to the EU budget, with the rebate taken into account. The EU do not pay the rebate to the UK in a separate transaction, it is deducted from the contributions the UK makes to the EU.[2]

The UK's estimated gross contribution (after the rebate) was £12.2bn in 2016/17.

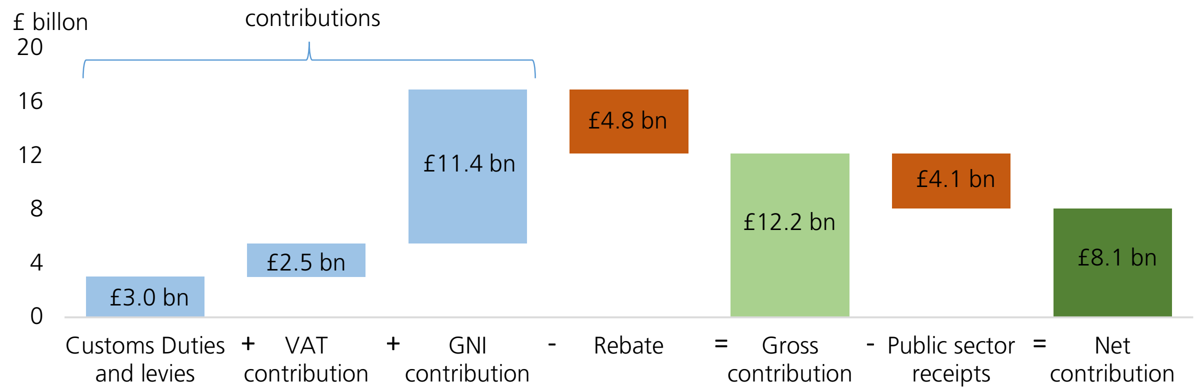
In keeping with all Member States, the vast majority of the UK's contribution came from its Gross National Income (GNI)-based contribution. The EU must run a balanced budget; that is, the EU's revenues must covers its spending. GNI contributions are used to balance the EU's budget, they make up the difference between the EU's spending and its other revenues.

The UK's public sector received an estimated £4.1bn of funding from the EU in 2016/17. The UK's net contribution, therefore, was £8.1bn.

EU receipts and the net contribution

The UK received an estimated £4.1 billion of public sector receipts from the EU in 2016/17. This means the UK's net contribution to the EU budget was £8.1 billion.

Chart 1. UK contributions to, and receipts from, the EU budget
£ billion, 2016/17



As the Library briefing [Brexit: UK Funding from the EU](#) discusses, the majority of the receipts received by the UK are for agriculture. The European Agricultural Guarantee Fund (EAGF) – which pays subsidies to farmers – is the largest fund.

The majority of the UK's receipts from the EU are for agriculture.

Much of the rest of the UK's EU receipts came from the European Structural Funds. The Structural Funds – largely made up of the

2 The rebate is paid a year in arrears. So the rebate applied in 2014 was calculated on the UK's net contribution in 2013.

European Regional Development Fund and European Social Fund – support economic development, skills, employment and training.

HM Treasury's measure of EU receipts does not include all the funding that UK organisations receive from the EU. HM Treasury include only funds allocated to the UK government to manage. Funds allocated directly to UK organisations by the European Commission, such as through Horizon 2020, are not included by HM Treasury.

Box 2: Who administers funding?

EU funding coming to the UK takes two forms:

- **Funds allocated to the UK government to manage** – this covers the majority of the EU's funding and is managed by national and regional authorities. In the UK, this is largely done through the structural and agricultural funds.
- **Funds allocated directly by the European Commission to UK organisations** – these funds are not allocated to Member States. In general, organisations apply directly to the Commission for funding from these streams, often on a competitive basis following calls for applications.

Table 1. UK Contributions to, and public sector receipts, from the EU budget, £ million

	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
UK contributions to the EU						
Customs duties and levies	2,205	2,171	2,200	2,263	2,314	3,020
VAT contributions	2,276	2,398	2,163	2,316	2,751	2,477
GNI contribution	11,218	12,303	13,845	14,154	12,570	11,440
Contributions	15,699	16,872	18,208	18,733	17,635	16,937
UK rebate	*-3,516*	*-3,172*	*-4,130*	*-4,811*	*-4,068*	*-4,757*
Gross contributions	12,184	13,699	14,079	13,921	13,567	12,180
Total Public Sector Receipts	4,771	4,022	3,856	4,690	2,811	4,079
Net Contribution	**7,413**	**9,678**	**10,223**	**9,231**	**10,756**	**8,102**

Source: HM Treasury, *Public expenditure statistical analyses 2017, Table C.1,* and previous editions

As table 1 shows, the UK's net contribution to the EU budget is fairly volatile from year to year. Aside from exchange rate volatility, there are reasons for this in terms of both receipts and contributions.

On the contributions side the UK's GNI-contribution fluctuates most noticeably. Member States' GNI contributions are used to ensure the EU's budget balances – that is, they cover the gap between the EU's spending and its non-GNI revenues. This means the GNI contribution is susceptible to changes in the EU's spending from one year to the next and changes in the EU's other sources of revenue, including any surplus carried over from the previous year.

On the receipts side the flow of funding from the EU is not consistent from one year to the next.

As the rebate is calculated on the UK's net contribution, it shouldn't be surprising, given the volatility in both contributions and receipts, that the UK's rebate also fluctuates.

Direct funding from the European Commission

Funds managed directly by the European Commission are generally aimed at improving competitiveness across the EU. They include funding for research and innovation (Horizon 2020), infrastructure (Connecting Europe Facility), education, training, youth and sport (Erasmus+), cultural and creative industries (Creative Europe) and support for small businesses to access finance and markets (COSME).

Data on the receipts received from these programmes are less timely, however in recent years they have been around £1 billion - £1.5 billion a year. If these are taken into account, the Treasury estimates that the UK's average net contribution to the EU budget was £7.1 billion between 2010 and 2014.[3]

UK organisations receive around £1bn - £1.5bn a year directly from the European Commission.

Box 3: The European Commission's calculation of the UK's budget contribution[4]

The European Commission publish data on the EU's spending in Member States and Member States' contributions to the EU budget. The Commission's approach is different to that of HM Treasury and, therefore, gives different figures:

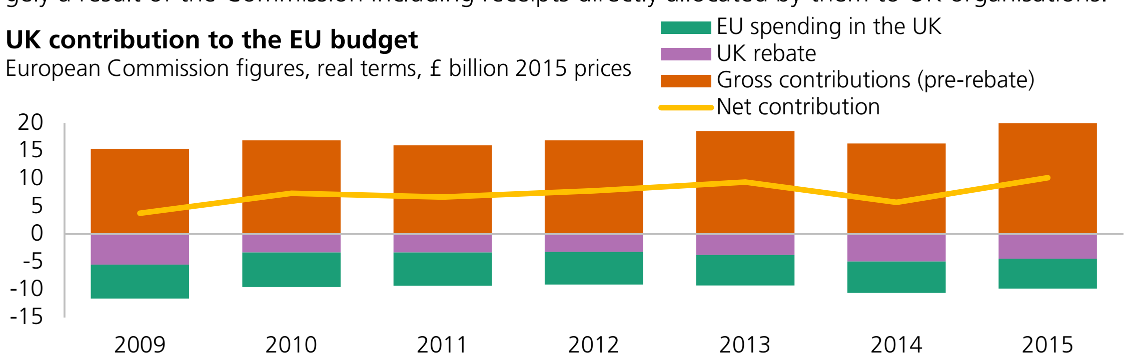
- the Commission includes all receipts going to the UK, including those the Commission directly allocates. These are not included in HM Treasury's figures (see section 1.2)
- the Commission attempt to match transaction to a particular EU budget year. HM Treasury's figures are based on cash flow within the year.

In addition, the figures presented in this briefing from HM Treasury are for financial years.

The chart below provides the Commission's data on the UK's net contributions. The Commission generally reports lower net contributions compared with HM Treasury. The lower net contributions are largely a result of the Commission including receipts directly allocated by them to UK organisations.

UK contribution to the EU budget

European Commission figures, real terms, £ billion 2015 prices



Member State comparisons

Member States' net contributions can be compared using the Commission's data. In 2015 the UK made the second largest net contribution to the EU budget in absolute terms, and the third largest net contribution per head of population.

Generally speaking, richer Member States are net contributors to the EU budget – they contribute more to the EU budget than they receive from it. Poorer states are generally net recipients – they receive more from the EU budget than they pay in. The 14 states with the lowest GNI per head of population are all net recipients from the EU budget. Section 3 of the Library briefing A guide to the EU budget provides further details.

[3] HM Treasury the long-term economic impact of EU membership and the alternative, Table 1.B)

[4] EC's EU expenditure and revenue 2014-2020, converted to £s using BoE's data

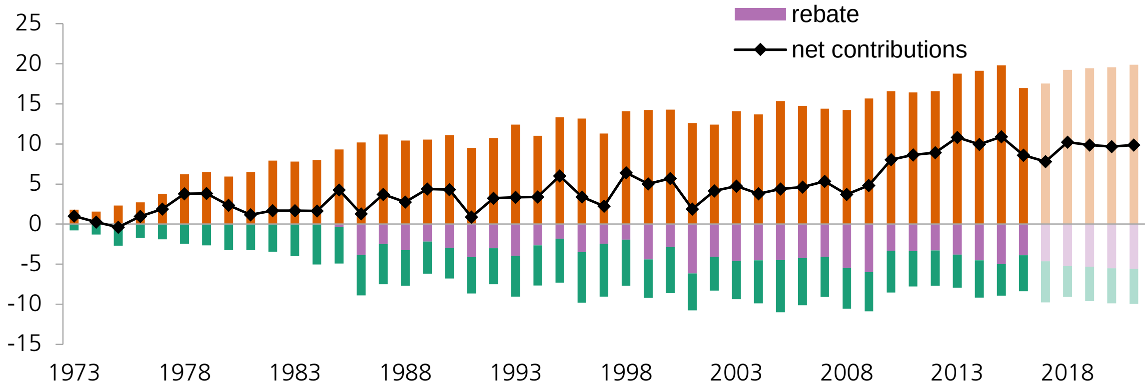
The UK's net contribution and forecast net contribution: 1973 - 2021

The chart below and tables 2 and 3 show the UK's contributions and receipts from the EU since 1973, using HM Treasury figures for calendar years. HM Treasury's figure for 2016 is an estimate as their outturn figure hasn't yet been published. As these are the Treasury's figures they do not include funding aollcated directly by the Commission to UK organisations.

The data include forecasts from the Office for Budget Responsibility (OBR) – the UK's public finances watchdog – for the years after 2015. The forecasts assume that the UK remains in the EU and contributes to its budget in the normal way. The forecasts are not an estimate of any payments the UK might make to the EU once it has left. The OBR took this approach as, when they made the forecast, they didn't have enough information about what the government wants from its future relationship with the EU, and what its chances of getting it are:

> As we do not have sufficient detail about the Government's negotiation preferences, or the chances of achieving them, we are not able to forecast how spending will be affected after the UK leaves the EU. We therefore make the fiscally neutral assumption that any reduction in transfers to the EU would be recycled into extra domestic spending.[5]

UK contributions to and receipts from the EU budget
real terms, £bn 2016 prices,1973-2021, OBR forecasts after 2016



5 OBR. Economic and fiscal outlook – November 2016, table 4.17 footnote 2

Table 2. UK net contributions to the EU/EC Budget 1973-2021. Forecasts after 2016.

£ million, cash

	Gross contribution before rebate	Negotiated refunds	Rebate	**Gross contribution (after rebate and refunds)**	Public sector receipts	**Net Contribution** *(Gross contribution - rebate & refunds - public sector receipts)*
1973	181			**181**	79	**102**
1974	181			**181**	150	**31**
1975	342			**342**	398	**-56**
1976	463			**463**	296	**167**
1977	737			**737**	368	**369**
1978	1,348			**1,348**	526	**822**
1979	1,606			**1,606**	659	**947**
1980	1,767	98		**1,669**	963	**706**
1981	2,174	693		**1,481**	1,084	**397**
1982	2,863	1,019		**1,844**	1,238	**606**
1983	2,976	807		**2,169**	1,522	**647**
1984	3,204	528		**2,676**	2,020	**656**
1985	3,940	61	166	**3,713**	1,905	**1,808**
1986	4,493		1,701	**2,792**	2,220	**572**
1987	5,202		1,153	**4,049**	2,328	**1,721**
1988	5,138		1,594	**3,544**	2,182	**1,362**
1989	5,585		1,154	**4,431**	2,116	**2,315**
1990	6,355		1,697	**4,658**	2,183	**2,475**
1991	5,807		2,497	**3,309**	2,765	**544**
1992	6,738		1,881	**4,857**	2,827	**2,030**
1993	7,985		2,539	**5,446**	3,291	**2,155**
1994	7,189		1,726	**5,463**	3,253	**2,211**
1995	8,889		1,207	**7,682**	3,665	**4,017**
1996	9,133		2,412	**6,721**	4,373	**2,348**
1997	7,991		1,733	**6,258**	4,661	**1,597**
1998	10,090		1,378	**8,712**	4,115	**4,597**
1999	10,287		3,171	**7,117**	3,479	**3,638**
2000	10,517		2,085	**8,433**	4,241	**4,192**
2001	9,379		4,560	**4,819**	3,430	**1,389**
2002	9,439		3,099	**6,340**	3,201	**3,139**
2003	10,966		3,559	**7,407**	3,728	**3,679**
2004	10,895		3,593	**7,302**	4,294	**3,008**
2005	12,567		3,656	**8,911**	5,329	**3,582**
2006	12,426		3,569	**8,857**	4,948	**3,909**
2007	12,456		3,523	**8,933**	4,332	**4,601**
2008	12,653		4,862	**7,791**	4,497	**3,294**
2009	14,129		5,392	**8,737**	4,401	**4,336**
2010	15,196		3,047	**12,150**	4,768	**7,382**
2011	15,356		3,143	**12,214**	4,132	**8,082**
2012	15,745		3,110	**12,636**	4,169	**8,467**
2013	18,135		3,674	**14,461**	3,996	**10,465**
2014	18,778		4,416	**14,362**	4,583	**9,779**
2015	19,560		4,914	**14,646**	3,883	**10,763**
2016e	16,996		3,878	**13,118**	4,503	**8,616**
2017[f]	17,800		5,200	**12,700**	4,700	**7,900**
2018[f]	19,900		4,000	**16,000**	5,400	**10,600**
2019[f]	20,500		4,500	**16,100**	5,600	**10,400**
2020[f]	21,000		4,700	**16,200**	5,900	**10,400**
2021[f]	21,800		4,800	**16,900**	6,100	**10,800**

Note:

[e]2016 are estimates, [f] figures for 2017 - 2020 are foreccasts rounded to the nearest £100 million

Forecasts are convered to £ using exchange rate of Q4 of previous year

Sources:

HM Treasury, *European Union Finances*, latest edition published February 2017, Cm 9400

HM Treasury, *European Union Finances*, previous editions

OBR, Economic and fiscal outlook - March 2017, supplementary fiscal table 2.27

OBR, Economic and fiscal outlook - March 2017, supplementary economy table 1.9

House of Commons Library calculations

Table 3. UK net contributions to the EU/EC Budget 1973-2021. Forecasts after 2016.

£ million, real (2016) prices

	Gross contribution	Negotiated refunds	Rebate	**Total contribution (after rebate and refunds)**	Public sector receipts	**Net Contribution** *(Gross contribution - rebate & refunds - public sector receipts)*
1973	1,797			**1,797**	784	**1,013**
1974	1,548			**1,548**	1,283	**265**
1975	2,320			**2,320**	2,700	**-380**
1976	2,721			**2,721**	1,739	**981**
1977	3,804			**3,804**	1,900	**1,905**
1978	6,228			**6,228**	2,430	**3,798**
1979	6,481			**6,481**	2,660	**3,822**
1980	5,930	329		**5,602**	3,232	**2,369**
1981	6,503	2,073		**4,430**	3,243	**1,188**
1982	7,941	2,826		**5,115**	3,434	**1,681**
1983	7,823	2,121		**5,701**	4,001	**1,701**
1984	8,010	1,320		**6,690**	5,050	**1,640**
1985	9,327	144	393	**8,789**	4,510	**4,280**
1986	10,182		3,855	**6,327**	5,031	**1,296**
1987	11,198		2,482	**8,716**	5,011	**3,705**
1988	10,447		3,241	**7,206**	4,436	**2,769**
1989	10,543		2,178	**8,364**	3,994	**4,370**
1990	11,107		2,966	**8,141**	3,816	**4,326**
1991	9,530		4,099	**5,432**	4,538	**893**
1992	10,740		2,998	**7,741**	4,506	**3,235**
1993	12,410		3,946	**8,464**	5,115	**3,349**
1994	11,044		2,651	**8,393**	4,996	**3,396**
1995	13,336		1,810	**11,526**	5,499	**6,027**
1996	13,166		3,477	**9,689**	6,303	**3,385**
1997	11,298		2,451	**8,847**	6,590	**2,258**
1998	14,099		1,925	**12,174**	5,750	**6,424**
1999	14,251		4,392	**9,859**	4,819	**5,039**
2000	14,281		2,831	**11,451**	5,759	**5,692**
2001	12,619		6,135	**6,484**	4,615	**1,868**
2002	12,427		4,080	**8,348**	4,215	**4,133**
2003	14,099		4,576	**9,523**	4,793	**4,730**
2004	13,675		4,510	**9,165**	5,389	**3,775**
2005	15,364		4,470	**10,895**	6,515	**4,379**
2006	14,756		4,238	**10,518**	5,876	**4,642**
2007	14,425		4,080	**10,345**	5,017	**5,328**
2008	14,248		5,475	**8,773**	5,064	**3,709**
2009	15,672		5,981	**9,691**	4,882	**4,810**
2010	16,600		3,329	**13,273**	5,209	**8,064**
2011	16,444		3,366	**13,079**	4,425	**8,655**
2012	16,605		3,280	**13,327**	4,397	**8,930**
2013	18,768		3,802	**14,966**	4,136	**10,830**
2014	19,119		4,496	**14,623**	4,666	**9,957**
2015	19,806		4,976	**14,830**	3,932	**10,898**
2016e	16,996		3,878	**13,118**	4,503	**8,616**
2017[f]	17,600		5,100	**12,500**	4,600	**7,800**
2018[f]	19,200		3,900	**15,500**	5,200	**10,200**
2019[f]	19,500		4,300	**15,300**	5,300	**9,900**
2020[f]	19,600		4,400	**15,100**	5,500	**9,700**
2021[f]	19,900		4,400	**15,400**	5,600	**9,900**

Note:

[e]2016 are estimates, [f] figures for 2017 - 2020 are forecasts rounded to the nearest £100 million

figures may not sum due to rounding

Forecasts are convered to £ using exchange rate of Q4 of previous year

Sources:

HM Treasury, *European Union Finances*, latest edition published February 2017, Cm 9400

HM Treasury, *European Union Finances*, previous editions

OBR, Economic and fiscal outlook - March 2017, supplementary fiscal table 2.27

OBR, Economic and fiscal outlook - March 2017, supplementary economy table 1.9

ONS. GDP deflator March 2017

House of Commons Library calculations

2. The UK’s rebate

As discussed previously the UK receives a rebate on its net contribution to the EU budget. The rebate was introduced to address the issue of the UK making relatively larger net contributions than other Member States. When the rebate was introduced, in 1985, the UK received relatively little from the EU budget: it had a small agricultural sector, but most EU[6] spending went on agriculture. At the same time the UK made relatively large contributions to the budget, despite being among the less well-off Member States at the time.

As the rebate is included in the EU’s regulation that determines Member States’ contributions it is essentially permanent: the regulation can only be changed if all Member States, including the UK, agree.

The rebate can only be changed if all Member States, including the UK, agree.

How does the rebate work?

Broadly speaking the formula used means that the UK’s net contribution is reduced by 66% relative to what it would be without rebate.[7] However, certain parts of the EU’s spending are excluded from the deduction including EU overseas aid, and non-agricultural spending in Member States that joined the EU after April 2004. This final exclusion, which was agreed by the UK, was phased in from 2009 to ensure that the UK contributed to the costs of enlarging the EU. The UK was, according to the then Prime Minister Tony Blair, “the strongest supporter of enlargement among all member states”.[8]

The basic concept of the rebate has remained the same since its inception, but changes to its calculation have been made over time as the EU and its methods for raising revenues have changed. The changes aim to keep the calculation similar to what it would have been had the overall system not changed since 1985.

The European Commission calculates the rebate on the basis of its estimates of the likely outturn for payments from the budget in-year and its estimates of Member States’ contributions to the budget. These are then corrected in light of actual outturn figures. Corrections may be made up to three years after the year to which the rebate relates, after which a final reckoning is made in the fourth year. The rebate is deducted from the UK’s contribution a year in arrears.

The rebate is deducted from the UK’s contribution a year in arrears.

Who pays for the rebate?

The other Member States cover the cost of the UK’s rebate. The cost of the rebate is based on each states’ share of EU GNI, but Germany, the Netherlands, Austria and Sweden only pay one quarter of their amount due. The reductions are paid for by the remaining Member States.

The European Parliament Research Service’s briefing The UK 'rebate' on the EU budget discusses the rebate further.

6 Or European Economic Community as it was then known

7 The rebate is calculated by taking the difference between the UK’s percentage share of contributions to the EU and the UK’s percentage share of EU receipts, multiplying this figure by 0.66 and then multiplying it by total spending.

8 HC Deb 19 December 2005 c1563-5

3. UK payments to the EU on and after Brexit

The UK voted to leave the EU on 23 June 2016. The UK will remain a member of the EU until its departure has been negotiated and will continue to contribute to the EU budget until it formally leaves. Once it has formally left, the UK may still make some payments to the EU.

A payment on leaving the EU

The EU expect the UK to make a payment to cover its share of the EU's financial commitments and liabilities when it leaves. This has been described in the media as an 'exit bill' or 'divorce bill'. The EU want a 'single financial settlement' and see the issue as a case of settling the accounts. The settlement is being discussed in the first phase of Brexit negotiations.

The UK Government recognises that the UK has financial obligations to the EU, and vice-versa, and that they need to be resolved. Any payment may be spread over a number of years.

Payments after the UK has left the EU

Once the UK has left the EU it may make payments to the EU to participate in some EU programmes. However, the Government's Brexit White Paper said that the UK would leave the EU's single market and wouldn't be expected to make payments in exchange for such preferential market access:

> As we will no longer be members of the Single Market, we will not be required to make vast contributions to the EU budget. There may be European programmes in which we might want to participate. If so, it is reasonable that we should make an appropriate contribution. But this will be a decision for the UK as we negotiate the new arrangements.[9]

The UK may still pay to participate in some EU programmes after it has left the EU.

Box 4: The EU institutions

European Parliament - Directly elected body with legislative, supervisory and budgetary responsibilities

European Council - Defines the general political direction and priorities of the EU.

Council (of the European Union) - Voice of EU member governments, adopting EU laws and coordinating EU policies.

European Commission - Promotes the general interests of the EU by proposing and enforcing legislation as well as by implementing policies and the EU budget.

Box 1 of the Library briefing A guide to the EU budget discusses the EU institutions in greater detail.

9 HM Government, *The United Kingdom's exit from and new partnership with the European Union*, Cm9417, February 2017, para 8.51

3.1 A payment on leaving the EU

The EU wants to deal with the payment, or exit bill, in a 'single financial settlement'. The settlement will cover the outstanding EU budget commitments and liabilities made while the UK was a member. The settlement will, according to the EU, also cover the termination of the UK's membership of EU institutions such as the European Investment Bank (EIB) and the UK's participation in EU funds and facilities that are outside of the EU Budget.

The European Commission's chief negotiator, Michel Barnier, has reportedly put the payment at close to €60 billion.[10] The estimated size of the payment is contingent on what financial commitments, liabilities and assets are included and how these are shared. For example, the Centre for European Reform – a broadly pro-EU think tank – has produced estimates that range from €24 billion to €73 billion.[11] Estimates of the net payment from the Institute of Chartered Accountants in England and Wales (ICAEW) range from €6 billion to €36 billion.[12] The FT calculated a gross payment of up to €100 billion.[13]

The range of estimates highlights the fact that almost every element of the potential payment is subject to interpretation. Ultimately any payment will be determined in exit negotiations. Negotiations will determine which financial commitments, liabilities, and assets, are to be shared, and how they are shared. The number of years that the payment will be paid over will also be agreed in negotiations.

The first phase of Brexit negotiations will aim to reach agreement on a payment, or schedule of payments, to settle the UK's accounts with the EU.

The European Council's position

The European Council say that a single financial settlement (the settlement) should be made to ensure both the EU and the UK respect the financial commitments made during the UK's membership.[14,15] The European Commission has fleshed this out in a position paper on the settlement.[16] The EU see the issue as the UK settling the accounts.

Brexit negotiations are being carried out in two phases. The first phase will disentangle the UK from the EU and the settlement is part of this phase. The second phase will deal with the future EU-UK relationship. The EU has said that Brexit negotiations will only move on to discussing the EU-UK future relationship, including areas such as trade, once 'sufficient progress' has been made on the first phase of negotiations.

10 House of Lords European Union Committee, *Brexit and the EU budget,* 4 March 2017, HL Paper 125, page 3
11 Centre for European Reform, The €60 billion Brexit bill: How to disentangle Britain from the EU budget, February 2017, page 10
12 ICAEW, Analysing the EU Exit Charge, May 2017
13 'Brussels hoists gross Brexit 'bill' to €100bn', *FT*, 3 May 2017
14 European Commission, Annex to the Recommendation for Council Decision authorising the opening of the negotiations for an agreement with the United Kingdom of Great Britain and Northern Ireland setting out the arrangements for its withdrawal from the European Union, 3 May 2017, section III.2.
15 European Commission, European Council (Art. 50) guidelines for Brexit negotiations, 29 April 2017
16 European Commission, Position paper transmitted to the UK: essential principles on the financial settlement, 12 June 2017

What should the settlement cover?

The European Council's view is that the settlement should cover all financial commitments undertaken while the UK was a member of the EU. This includes commitments related to:[17]

- the European Union's Budget;
- terminating the UK's membership of EU bodies such as the European Investment Bank (EIB) and European Central Bank (ECB);
- the UK's participation in specific EU funds and facilities such as the European Development Fund – the EU's programme for support developing countries – and the Facility for Refugees in Turkey.

All liabilities including contingent liabilities should, according to the European Council, be included in the settlement. Contingent liabilities are potential liabilities that may occur depending on the outcome of an uncertain event in the future.

Box 5: Example of a contingent liability in the EU budget

The European Financial Stabilisation Mechanism

The European Financial Stabilisation Mechanism (EFSM) was created in 2010 as a temporary fund to provide loans to EU Member States in financial difficulty. The EFSM uses the EU budget as a guarantee to borrow money on financial markets, which it then subsequently lends to countries who require the funding.

If the countries who receive EFSM loans fail to repay them, then the EU budget bears the cost. If, as a result of this, additional money is required to fund the EU budget, further contributions from EU Members may be required. This is where the UK currently has a contingent liability.

What do the Council want to agree?

The Council say that an agreement on the settlement should include:[18]

- a calculation of the amount the UK is required to pay to cover its financial commitments to the EU budget and other EU institutions;
- an annual schedule of payments;
- rules to ensure UK beneficiaries of EU funding receive funding committed to them;
- rules to address the UK's share of the contingent liabilities of the EU Budget or institutions such as the EIB.

17 European Commission, Position paper transmitted to the UK: essential principles on the financial settlement, 12 June 2017
18 ibid

Box 6: European Commission's position paper on the settlement

The European Commission has produced a paper setting out the EU's position on the settlement.[19] The position paper fleshes out ideas put forward earlier in the Council's negotiating directives.[20] It is part of the documents published for the first phase of Brexit negotiations.

The paper says that the UK must honour its share of the financial commitments undertaken while it was a member of the EU. For instance, the UK agreed to the EU's spending plans and committed to funding them by agreeing revenue raising measures, and the Commission believes these commitments should be met.

On the same basis, the paper says the UK should continue to benefit from EU funding programmes until the programmes close. This means that the UK would continue to receive funding in areas such as economic development, agriculture and research and innovation until the current funding period, 2014 – 2020, ends. Continued participation would require the UK to obey the EU's legal rules for the programmes.

The position paper agrees with the European Council's view that the settlement should cover:

- the UK's participation in the EU Budget
- termination of the UK's membership of EU bodies and institutions, such as the European Investment Bank
- the UK's participation in specific EU funds and facilities, such as the facility for Refugees in Turkey.

The Commission suggests that the UK's share of outstanding EU Budget commitments should be based on the proportion of total contributions to the EU Budget that were from the UK over 2014-2018. The UK's rebate would be included when determining the UK's share of contributions to the EU Budget. In recent years the UK's share has been around 13%.[21]

The Commission says that the settlement should be determined and made in euros, and that a schedule of payments should be established with the aim of "mitigating the impact of the United Kingdom withdrawal on the budget for the Union and on its Member States."

The position paper goes into more detail on areas such as what parts of the EU Budget should be included in the settlement, and how the end of the UK's membership of the EIB should be ended. The Library briefing Brexit: the exit bill provides more detail on what the position paper says on these and other areas.

The UK Government's position

The UK Government has made no formal response to the European Council's position or the Commission's position paper. However, the UK Government has recognised that the UK has financial obligations to the EU, and vice-versa, and that they need to be resolved:

> On the financial settlement, as set out in the Prime Minister's letter to President Tusk, the Government have been clear that we will work with the EU to determine a fair settlement of the UK's rights and obligations as a departing member state, in accordance with the law and in the spirit of our continuing partnership. The Government recognise that the UK has obligations to the EU, and the EU obligations to the UK, that will survive the UK's withdrawal—and that these need to be resolved.[22]

[19] European Commission. Position paper transmitted to the UK: essential principles on the financial settlement, 12 June 2017

[20] The Council of the European Union, Negotiating directives for Article 50 negotiations, 22 May 2017

[21] See HM Treasury, European Union Finances 2016, February 2017; and previous editions.

[22] HC Deb.13 July 2017:c15-16WS

David Davis MP, Secretary of State for Exiting the European Union, has said that the UK will at first probe and challenge the EU's position on the settlement during negotiations. The UK may then publish an alternative proposal:[23]

> For something like the financial paper, we will go through it in session and debate it with the Commission. At the end, we may well publish an alternative proposal, but at the moment the proper approach, to get the right outcome in the negotiation, is to challenge what it is doing.
>
> At the end of the second round of negotiations, the BBC reported a Downing Street spokesman as saying that there are no plans to produce a position paper on the financial settlement.

Previously David Davis said that the UK will obey its legal obligations, but rejected speculation of the UK making a large payment to the EU.[24]

On 29 March 2017, Prime Minister Theresa May letter to Donald Tusk triggering Article 50 said the negotiations should determine a 'fair settlement' of the UK's obligations as a "departing member state, in accordance with the law and in the spirit of the United Kingdom's continuing partnership with the EU".[25]

What might the payment cover?

The EU has a range of different commitments and liabilities. Below, we briefly discuss the most significant. Negotiations will determine which of these will be included in the UK's financial settlement and how the UK's share will be calculated.

EU budget outstanding commitments

The EU, in their annual budgets, commit to some future spending without making payments to recipients at the time. The commitments will become payments in the future.

Currently the EU has over €200 billion of outstanding commitments which have not yet been paid.[26] The EU refer to outstanding commitments as reste à liquider (RAL).[27] It is the difference between spending that has been authorised and the amounts that have been paid out. Some of the RAL will be committed to the UK.

The Commission's position paper says this is an area it expects the settlement to cover.

23 House of Lords Select Committee on the EU, Uncorrected oral evidence: David Davis evidence session, 11 July 2017, Q2

24 'David Davis rejects claim of €100bn Brexit divorce bill', The Guardian, 3 May 2017; Committee on Exiting the European Union Oral evidence: The UK's negotiating objectives for its withdrawal from the EU, HC 1072, Q1411; "Brexit divorce bill will be 'nothing like' tens of billions of pounds, David Davis says", *The Independent,* 27 March 2017

25 Prime Minister's letter to Donald Tusk triggering Article 50, 29 March 2017, page 4

26 House of Lords EU Financial Affairs Sub-Committee, uncorrected oral evidence, 14 December 2017, pages 8 – 9

27 From the French for 'yet to be paid'.

EU budget 2014 to 2020

As we discuss in our briefing A guide to the EU budget, the EU's spending has been planned for the years 2014 to 2020.

The planned spending includes programmes for economic development, skills, cohesion, agriculture and asylum & migration. Much of the spending has been legally committed by the EU to provide certainty for the recipients, although it might not yet have been allocated through the EU budget process. To be clear, this spending is not part of the RAL as it hasn't entered into one of the EU's annual budgets yet.

The Commission's position paper says this is an area it expects the settlement to cover.

The EU's balance sheet: liabilities

The EU has liabilities of €226 billion and assets of €154 billion, at the end of 2015.[28] The EU wants the UK to cover it share of liabilities. The UK is likely to argue that if it is to cover its share of liabilities then it should receive a share of the EU's assets (see below for more).

Although the EU does have other liabilities – including those related to financial instruments – staff pension liabilities are the most mentioned in discussions of the UK's 'exit bill'. The EU has pension liabilities of €64 billion:[29] whether, and how, these might be shared with the UK isn't clear. As with everything discussed in this section the detail will be worked out in exit negotiations.

The Commission's position paper says this is an area it expects the settlement to cover. The Commission only expects liabilities which are not balanced by corresponding assets to be included.

The EU's balance sheet: contingent liabilities

Some liabilities are dependent on an uncertain event happening in the future. These are known as contingent labilities – they are contingent on something happening.

The EU has contingent liabilities of €28 billion at the end of 2015. Most relate to guarantees to loans granted by the European Investment Bank.

The Commission's position paper says this is an area it expects the settlement to cover.

What might reduce the size of the payment?

So far we have considered items that the EU may expect the UK to make a payment for when it exits. The UK may expect the size of the payment to be reduced by some other items.

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[28] European Commission, Consolidated annual accounts of the EU, Financial year 2015, July 2016, page 31

[29] European Commission, Consolidated accounts of the European Union, Financial Year 2015, 11 July 2016, page 32

The EU's balance sheets: assets

If the UK is required to contribute to the EU's liabilities, the UK Government may expect to benefit from a share of the EU's assets. The EU's assets include buildings, equipment and financial investments.

Again, whether the UK should receive a share of any of these assets is a matter for negotiations. The European Council's negotiation guidelines do not mention sharing assets, nor does the Commission's position paper.

The EU has larger liabilities than assets, so if these are shared it is probable that the UK would make a payment to the EU rather than receive one from the EU.[30] However, this depends on precisely what it shared.

Terminating European Investment Bank (EIB) membership

The UK has a 16% share in the EIB. As EIB ownership is restricted to EU members the UK may have to sell its stake to other Member States, unless the rules are changed to allow it to continue to participate.

An estimate from the ICAEW – an accountancy membership organisation – suggests the UK's share of the EIB could be worth around €11 billion by March 2019.[31]

The Commission's position paper discusses returning the UK's investment in the EIB. It also discusses returning the UK's investment in the European Central Bank (ECB). The Commission proposes that:

- the UK's capital in the EIB be paid back once all the EIB's outstanding loans, at the time of UK withdrawal, have concluded.
- the UK's capital in the ECB should be reimbursed on withdrawal.

The rebate

The rebate is taken off the UK's contribution a year in arrears. This means that when the UK makes its final contribution as a Member State it may expect a rebate payment the following year. The rebate may be used to reduce any 'exit bill'. The OBR forecasts that the rebate would be worth over £5 billion in 2019 and 2020.[32]

What is the legal position of the exit bill?

There is some debate over whether the UK is legally liable for any of the payments described above. A Lords Committee recently considered the issue and found that the most persuasive argument was that the UK would not be legally liable for any payment. However, the same committee also concluded that if the UK were to simply leave without making any payments the economic and political consequences could be 'profound':

30 European Court of Auditors, Annual Reports concerning the financial year 2015, 13 October 2016, para 1.5
31 ICAEW, Analysing the EU Exit Charge, May 2017, page 7
32 OBR. Economic and fiscal outlook – March 2017, supplementary fiscal tables, table 2.27

> On the basis of the legal opinions we have considered we conclude that, as a matter of EU law, Article 50 TEU [the Treaty on the European Union] allows the UK to leave the EU without being liable for outstanding financial obligations under the EU budget and related financial instruments, unless a withdrawal agreement is concluded which resolves this issue.
>
> Individual EU Member States may seek to bring a case against the UK for the payments of outstanding liabilities under principles of public international law, but international law is slow to litigate and hard to enforce. In addition, it is questionable whether an international court or tribunal could have jurisdiction.
>
> However, the political and economic consequences of the UK leaving the EU without responding to claims under the EU budget are likely to be profound. If the UK wants a preferential trading relationship with EU, including a transitional arrangement, the EU partners may well demand a financial contribution post-Brexit.[33]

The Lords Committee received conflicting evidence about the legal position and its conclusion was based on what it felt was the most persuasive argument.[34] Since the Committee published its report some have questioned the conclusion reached on the legal position of the UK's financial obligations.[35]

3.2 Future payments: access to programmes and the single market

After its exit, the UK could still contribute to the EU to access its programmes and for preferential access to the single market.

Prime Minister Theresa May expects financial contributions to the EU, after exit, to be somewhat lower than current budget contributions; Mrs May has said that:

- the UK may continue to take part in some EU programmes, and would contribute to the EU for doing so.
- the UK will leave the single market, so will not have to make contributions for membership.[36]

Participating in programmes directly managed by the European Commission

The UK may continue to participate in some of the funding programmes directly managed by the European Commission. The UK would pay to participate in the programmes.

33 House of Lords European Union Committee, *Brexit and the EU budget,* 4 March 2017, HL Paper 125, paras 135 - 137
34 ibid, paras 98 - 160
35 For instance see, Blog of the European Journal of International Law, The Brexit Bill and the Law of Treaties, 4 May 2017
36 10 Downing Street, The government's negotiating objectives for exiting the EU: PM speech, 17 January 2017

Non-EU countries, who have some relationship with the EU, already take part in some of the Commission's funding programmes. For instance, Turkey – a candidate country for EU membership – participates in programmes including Horizon 2020, Erasmus+, Creative Europe, COSME, EaSI.[37] Norway – a member of the European Economic Area (EEA) – participates in at least 12 EU programmes.[38]

Some non-EU countries already take part in European Commission funding programmes.

Non-EU countries often contribute to European Commission programmes they participate in on the basis of the relative size of their national income. Beyond financial contributions, the Commission may have other requirements for some programmes, such as an agreement on free movement of people. For instance, Switzerland's participation in Horizon 2020 – the EU research and innovation programme – covered only part of the programme until it met the EU's requirements on free movement of people.[39] However, non-EU countries membership of Horizon 2020 does not follow one single model.

The UK's future participation in any European Commission programmes will be determined in exit negotiations. The precise terms – including the cost involved – will be a matter for negotiation.

Box 7: EU economic development and agricultural funds

Currently, the majority of the funding the UK receives from the EU is allocated directly to the UK to manage. This funding does not come from the European Commission's directly managed programmes, which are discussed above.

The UK directly manages funding for economic development including the European Regional Development Fund[40] and the European Social Fund and the agricultural funds.

It is unlikely that the UK will take part in these funds after exit, or after any transition period has ended. Non-EU countries do not take part in the economic development funds nor the agricultural funds.

Box 8: The European Economic Area

The European Economic Area (EEA) is made up of all EU Member States plus Norway, Iceland and Liechtenstein, who are often referred to as the non-EU EEA countries.

The EEA Agreement extends the EU single market and free movement of goods, services, people and capital, together with laws in areas such as competition policy, state aid, consumer protection and environmental policy to include Norway, Iceland and Liechtenstein.

Non-EU EEA countries are outside of the common customs union so can set their own trade policies with countries outside the EEA.

The Library briefing *Brexit: trade aspects* discusses the EEA further.

37 Turkey – European Union Association, EU Programmes and Agencies to which Turkey Participates
38 Norway mission to the EU, Norway's participation in EU programmes and agencies, 10 August 2016
39 For more see page 32 of the Library briefing UK Funding from the EU.
40 Some can benefit from INTERREG funding, which is funded from the European Regional Development Fund. They can do so through bordering countries, but only if the bordering countries apply for the funding.

Preferential access to the EU's single market

The Prime Minister has stated that the UK will not seek membership of the single market. However, with negotiations yet to begin, and significant uncertainty surrounding them, it is worth considering the contributions non-EU countries make in exchange for preferential access to the single market.

Some non-EU countries contribute grants to the poorer EU Member States in exchange for preferential access to the single market.

Non-EU EEA members (see Box 5) have significant access to the single market with some exceptions in agriculture and fisheries. The non-EU EEA members – Norway, Iceland and Liechenstein– contribute grants to the poorer EU Member States in exchange for preferential access to the single market.[41] Norway – by far the biggest of the non-EU EEA countries – also has an agreement with the EU to provide separate grants, which are commonly known as Norway Grants. Norway will provide €1.3 billion through Norway grants between May 2014 and April 2021 and around €1.5 billion through the EEA grants.[42]

Switzerland has limited access to the single market. It has tariff- and quota-free access to the EU's markets for manufactured goods and has negotiated access for particular service sectors. Switzerland provides grants to countries that have joined the EU since 2004.[43] Approximately £900 million of grants over five years have been committed.[44]

The Lords European Union Committee considered whether the UK might pay for greater access to the single market. They concluded that the extent of any payment will be a matter for negotiation and will involve a series of trade-offs:

> The question of whether the UK will be required to make a payment in return for market access will be a matter for negotiation, and is likely to involve trade-offs between the level of access sought, the structure and level of other payments and more general political considerations. If the UK refuses to accept free movement of persons or the jurisdiction of the CJEU [Court of Justice of the European Union], the price that it is asked to pay could be proportionately higher than that demanded of Norway [who do accept free movement and the CJEU]. The Government will have to consider any proposals in the round, weighing any payment included in a wider trade deal against the economic benefits the UK stands to gain from continued market access.[45]

41 European Commission, protocol 38C on the EEA Financial Mechanism (2014-2021), February 201
42 European Commission, Agreement between the Kingdom of Norway and the European Union on a Norwegian financial mechanism for the period 2014-2021, Annex, February 2016
43 Confederation Suisse, The Swiss contribution in brief [accessed on 23 January 2017]
44 IFS. Brexit and the UK's Public Finances, May 2016, pages 15-16
45 House of Lords European Union Committee, *Brexit and the EU budget,* 4 March 2017, HL Paper 125, para 187

3.3 Further information

- The Centre for European Reform, The €60 billion Brexit bill: How to disentangle Britain from the EU Budget, February 2017
- House of Lords European Union Committee, Brexit and the EU budget, 4 March 2017, HL Paper 125
- ICAEW, Analysing the EU Exit Charge, May 2017
- Bruegel, Divorce settlement or leaving the club? A breakdown of the Brexit bill, 30 March 2017
- Institute for Fiscal Studies, Brexit and the UK's Public Finances, May 2016, section 2.2
- House of Commons Library, Brexit: UK Funding from the EU, 29 December 2016, section 6 and section 7

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