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BREXIT:
WILL THE UK HAVE TO PAY TO LEAVE THE EU?

– THOUGHT LEADERSHIP

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BREXIT

Will the UK have to pay to leave the EU?

Who should pay what as a result of the UK's withdrawal from the EU raises difficult questions that, unless resolved, have the potential to render the negotiations on the UK's future relations with the EU substantially more complex.

Executive summary

The figure of €60 billion as the sum that the UK must pay the EU on the UK's withdrawal from the EU has gained currency, but the position is anything but clear. In particular:

- The argument for payment by the UK of a sum as large as €60 billion rests on the UK having a continuing obligation to contribute to liabilities to which the EU committed itself prior to the UK's departure even if payment does not fall due until after departure. The EU's budgets include both payment appropriations for each year and (higher) commitment appropriations that include payments falling due in later years.
- The argument for the UK not being obliged to pay a sum as large as €60 billion rests on the EU's commitments being just that – obligations of the EU, a legal entity in its own right, not of its member states. Member states might have an obligation under the EU's treaties to pay money into the EU's budget generally, but article 50(3) of the TEU expressly provides that the EU's treaties cease to apply to a former member state on its withdrawal from the EU. There is no commitment by member states, present or past, to fund specific projects.
- The UK might also ask for a payment representing the share of the EU's assets that the UK's past contributions have financed. The EU's balance sheet shows a negative balance of €72.5 billion, covered, amongst other entries, by €77.1 billion "to be called from Member States".
- The EU's future comitments include its pension obligations (shown at €64 billion in the EU's balance sheet) as well as payments under its social and regional initiatives aimed at generating growth in poorer areas of the EU.
- The EU's annual budgets must balance. The UK is a net contributor to the EU's budget. If UK payments cease, the EU will face, probably in 2019, a shortfall in its budget, which will have to be met either by increased payments or by a reduction in spending.
- The UK and the EU will hopefully reach an agreement on payments, even though the principles are far from easy and quantification even less so. A failure to agree could sour other negotations, including over future trading arrangements between the UK and the EU.
- If the EU and the UK cannot agree, the dispute might need to be resolved by a tribunal. The CJEU might consider that it has jurisdiction, though that is unlikely to be acceptable to the UK. An ad hoc international tribunal might be best, if that is legally possible for the EU.

Introduction

The primary focus of debate about Brexit has been on what arrangements the UK might enter into with the EU for the period after the UK's withdrawal from the EU, whether it be remaining within the internal market, effectively remaining within the customs union, establishing a wholly new arrangement based on equivalence, or something else altogether (and that's before transitional arrangements reach the agenda). But before the discussion can reach the post-Brexit deal (or, if the UK has its way, alongside that discussion), the UK and the EU must agree the terms for the UK's withdrawal from the EU. A fundamental aspect of the withdrawal deal will be what, if anything, the UK must pay the EU or the EU must pay the UK as a result of withdrawal. This seems likely to be a difficult negotiation – financially, politically and legally – and one that could colour all other negotiations. A failure to agree the finances of withdrawal may make it impossible to move forward to other matters.

The messages being fed to the media about the finances of withdrawal indicate that there could be a chasm between the two sides' opening positions, though no one can be sure how much is pre-negotiation positioning (an attempt at "anchoring", in the language of psychologists like Daniel Kahneman) and how much is serious. Sources close to the EU's Brexit negotiators have suggested that the EU could demand a payment of up to €60 billion from the UK as the price of withdrawal, or three times the UK's gross contribution to the EU in 2016 and an even higher multiple of the UK's net contribution. In contrast, sources close to the UK Government have suggested that the UK is looking carefully at the EU's assets in order to demand on departure the UK's fair share of their value.

The legal position regarding payments on withdrawal is anything but clear. In the customary way of the EU, the amount of any payment, whether by the UK or by the EU, on the UK's departure is likely to be resolved in a late-night horse trade (though there are few obvious gift horses in sight). Ultimately, if agreement cannot be reached, the issue might have to be decided by an international legal tribunal.

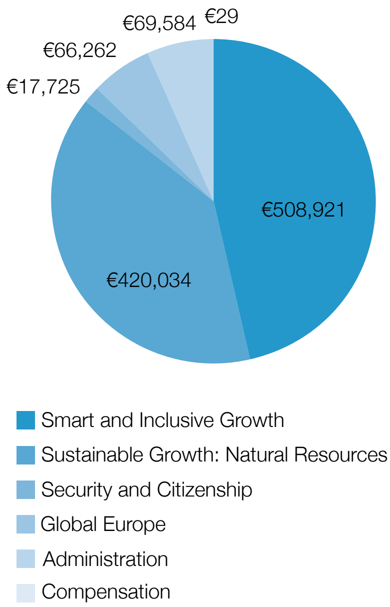
In this briefing, we look at the arguments surrounding possible payments on the UK's departure from the EU. This must, alas, begin with an outline of the EU's arcane system of financing before going on to the implications of Brexit.

The EU's expenditure

The starting point for EU expenditure is the multiannual financial framework (MFF) required by article 312 of the Treaty on the Functioning of the European Union. This must be agreed unanimously by the European Council (ie by all the member states) and approved by majority in the European Parliament. The MFF does not set expenditure as such but provides the ceilings for expenditure with which the EU's annual budgets must then comply. The ceilings come in two forms: a ceiling for "commitment appropriations", ie expenditure to which the EU commits itself but which might actually lead to payments in subsequent years; and a (lower) ceiling for "payment appropriations", ie cash out of the door.

The most recent MFF is laid down in Council Regulation 1311/2013 (EU, Euratom) for the seven years from 2014 to 2020, ie ending some 21 months after the UK will leave the EU if the UK's notice of intention to withdraw is, as the UK Government wants, given in March 2017 (unless the two year period is extended by unanimous agreement under article 50(3) of hte TEU). Over the entire seven-year period, the MFF provides, in its original form, for commitment appropriations of €960 billion and for payment appropriations of €908 billion (the figures are subject to subsequent adjustment under article 6 for inflation and other technical matters). This is some 1% of the aggregate gross national income (GNI) of the EU's member states; the member states themselves spend over 48% of the EU's GNI. The MFF allocates the overall expenditure to each of the calendar years in the seven-year period on a slightly increasing basis, so, for example, the expenditure for 2014 was set at 13.99% of the seven-year total, and the expenditure for 2020 at 14.61%.

The three largest expenditure items shown in the MFF are: "smart and inclusive growth" (47%), which aims to help under-developed EU regions and disadvantaged sections of society;



EU commitment appropriations, 2014- 2020 (€ millions)

Source: European Commission, EU Budget 2015 Financial Report, Annex 1, MFF 2014-2020 adjusted Technical Adjustment for 2016 "sustainable growth: natural resources" (39%), the bulk of which relates to agriculture; and "administration" (6%).

The MFF can be revised "in the event of unforeseen circumstances" (article 17(1), but the revision must be in accordance with the EU's "own resources" decision, discussed below). There is specific provision in the MFF Regulation (article 21) for revision of the MFF in the event of enlargement of the EU, but the Regulation does not contemplate shrinkage.

Having set the ceilings for the EU's expenditure in the MFF Regulation, the EU then adopts under article 314 of the TFEU annual budgets for each calendar year, again including payments and commitments. This requires the Commission to submit a draft budget to the Council and the Parliament by 1 September in the preceding year (the Commission in fact approved its draft budgets for 2015 and 2016 on 24 June in each preceding year). The Council must then adopt its position on the draft budget, by qualified majority voting (not the unanimity required for the MFF), by 1 October. If the European Parliament approves the Council's position, the budget is adopted, but if the Parliament declines to do so there is a complex conciliation procedure aimed at securing agreement between the two institutions. If agreement is not reached by the start of the financial year, the old budget rolls forward on a monthly ("twelfths") basis (article 315 of the TFEU).

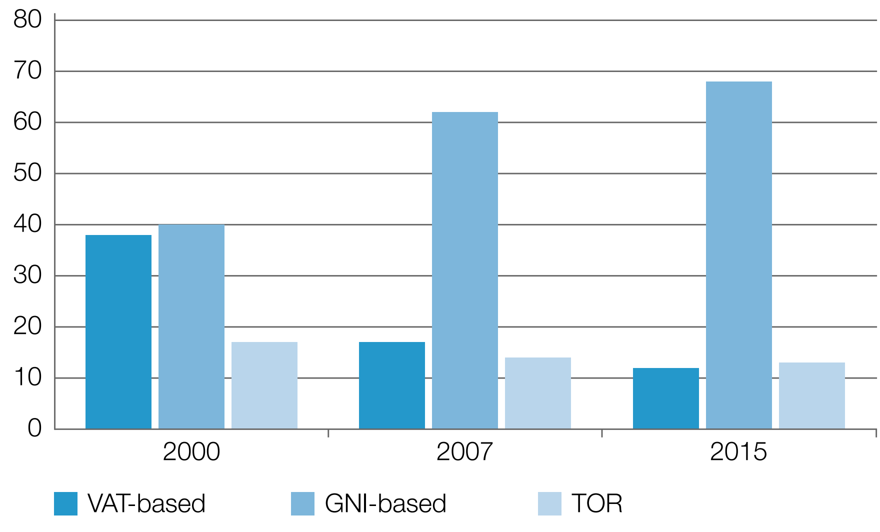
While the MFF operates at a very high level (effectively one table, covering half a page at the end of the Regulation), the EU's annual budgets condescend to every kind of detail. The budget for 2016 runs to 2,283 pages in the EU's Official Journal (2016, L48).

The EU's income

The EU's annual budget must balance (article 310(1) of the TFEU). Unlike its member states, the EU cannot run a budget deficit. The EU's payments in each year must therefore be matched by its income, most of which is referred to as the EU's "own resources". The revenue raised by the EU is applied to all the EU's expenditure; there is no hypothecation of particular income to particular expenditure, whether on a national or any other basis (article 6 of Council Decision 2014/355).

The EU has three main sources of income, set out in Council Decision 2014/335, the amount of which must be estimated in the annual budget prepared by the Commission in order to balance the budget. These three sources are as follows:

- "traditional own resources", namely customs duties levied on trade coming into the EU from third countries. Member states keep 20% (down from 25%) of what they collect in customs duties "by way of collection costs", though in practice this retention far exceeds actual collection costs;
- 0.3% of the each member state's "harmonised VAT assessment basis".



EU "own resources"

Source: European Commission, EU Budget 2015 Financial Report, Annex 2b

Each member state's VAT assessment basis is capped at 50% of its GNI, but the assessment basis is only distantly related to a member state's actual VAT receipts. Indeed, the EU's Court of Auditors has described the system as "complex to the point of incomprehensibility";

- A balancing payment decided in the annual budgetary process by reference to each member state's gross national income, or GNI.

There are then adjustments to the payments that the uniform application of the own resources rules would otherwise require from particular member states. So, for example, Germany, the Netherlands and Sweden pay the VAT-based own resource at 0.15% rather than 0.3%, and Denmark, the Netherlands and Sweden receive reductions on their GNI contributions.

The largest adjustment is the "correction mechanism" in favour of the UK, now in article 4 of the Council's own resources decision. This reduces the UK's net payments to the EU, and was originally set at 66% of the difference between the UK's harmonised VAT base (then the EU's main source of income) and the UK's receipts from the EU's budget. The exact manner of calculation of the correction has been adjusted since (eg to take into account the subsequent joiners to the EU and the changing nature of EU funding) but the basic approach remains similar.

The reduction in the EU's income as a result of the UK's rebate is, in the main, met by the other member states rather than by lowering EU expenditure. However, to add to the complexity, some member states (eg Germany, the Netherlands, Austria and Sweden) receive rebates on the payments otherwise due from them to compensate the EU for the UK's rebate.

The proportion of its revenue that the EU receives from its three main sources of income has varied over time. For example, in 1988 around 60% of the EU's income came from VAT-based own resources and 28% from traditional own resources. Now traditional own resources represent some 13% of the EU's income, VAT-based own resources 12% and the GNI-based own resources about 70%. This reflects a move to a more redistributive approach to EU funding – from the richer member states to the poorer – which neither of the other funding sources can achieve. The adjustments to the member states' payments do, however, generally have the effect of reducing the payments by those members that are net contributors to the EU's budget.

Overall, the UK is a net contributor to the EU's budget. The Institute for Fiscal Studies put the UK's gross contribution in 2014 at £14.4 billion (£12.9 billion for 2015), its net contribution after deducting EU payments received by the UK public sector at £9.8 billion (£8.5 billion for 2015), and its net contribution after deducting EU payments received by the UK public sector and EU payments received by other organisations and businesses in the UK at £5.7 billion. The House of Commons Library has estimated the UK's average net contribution between 2010 and 2014 at £7.1 billion per year. The loss of this net income to the EU as a result of the UK's withdrawal will require the EU to finesse its budget carefully in order to achieve the required balance.

Withdrawal and the EU's treaties

Article 50(2) of the Treaty on European Union requires the EU to negotiate and conclude an agreement with the departing state "setting out the arrangements for its withdrawal", but gives no hint as to what those arrangements should be, the basis upon which they should be approached or, indeed, what happens should nothing be agreed.

The only word about the consequences of withdrawal, whether for the departing member state or for those that remain, is in article 50(3) of the TEU. This merely provides that the EU's treaties cease to apply to the withdrawing state on entry into force of a withdrawal agreement or, failing that, two years after the withdrawing state has given notice of its intention to withdraw. Article 50(3) might therefore suggest that departure leads to a dropping of hands, a cliff edge: prior to the departure day, the withdrawing member remains a full participant in the EU, with all the rights and obligations (including as to payments and receipts) of a member state; on the departure date, it ceases to have any rights or obligations

> **"(2) A Member State which decides to withdraw shall notify the European Council of its intention. In the light of the guidelines provided by the European Council, the Union shall negotiate and conclude an agreement with that State, setting out the arrangements for its withdrawal, taking account of the framework for its future relationship with the Union...**
>
> **(3) The Treaties shall cease to apply to the State in question from the date of entry into force of the withdrawal agreement or, failing that, two years after the notification referred to in paragraph 2..."**
>
> (Article 50 of the Treaty on European Union)

“(1) Unless the treaty otherwise provides or the parties otherwise agree, the termination of a treaty under its provisions..:

(a) Releases the parties from any obligation further to perform the treaty;

(b) Does not affect any right, obligation or legal situation of the parties created through the execution of the treaty prior to its termination.

(2) If a State denounces or withdraws from a multilateral treaty, paragraph 1 applies in the relations between the State and each of the other parties to the treaty from the date when such denunciation or withdrawal takes effect.”

(Article 70 of the Vienna Convention on the Law of Treaties)

under the EU’s treaties. The UK’s obligation to pay into the EU’s coffers arises under the Council’s own resources decision, made under the treaties, and that obligation will therefore cease on the UK’s withdrawal from the EU.

This does not, however, necessarily mean that withdrawal will relieve the UK of all future payment obligations. Article 70 of the Vienna Convention on the Law of Treaties could be relevant as representing customary public international law in the area. Article 70 states that, unless a treaty provides otherwise, withdrawal from a treaty under its provisions “releases the parties from any obligation further to perform the treaty” but does “not affect any right, obligation or legal situation of the parties created through the execution of the treaty prior to its termination”.

Article 50(3) of the TEU reflects the first aspect of article 70 of the VCLT (no future obligations), but does not expressly exclude the second aspect of article 70 (continuation of accrued rights and obligations) – it would only do so if article 50(3)’s silence is treated as “providing otherwise”. If the UK were to fail to make a payment that fell due prior to Brexit day, it seems likely that the UK would continue to be obliged to make that payment despite departure. Departure would not generally absolve a party retrospectively from its prior obligations. But what if the payment, though due prior to departure, was calculated by reference to a period that straddled the departure date? Presumably, the pro-rating of payments is possible.

The position becomes more difficult when trying to assess what, if any, EU payment obligations on the UK have accrued within the meaning of the VCLT prior to the UK’s withdrawal from the EU but which only fall due for payment afterwards and, if there are any, whether the UK will be obliged to meet them despite its withdrawal from the EU.

The EU’s expenditure for any particular year is split between payments and commitments. The commitments made by the EU typically run for up to three years into the future, but can be longer term. Where the EU has made a commitment that extends past Brexit day, the EU’s argument, based on article 70 of the VCLT, must be that this creates a matching obligation on the UK accruing prior to departure to provide the EU with the necessary funds after departure. Departure is therefore necessarily a gradual process. The inverse of this argument is that if the UK has a continuinng obligation to provide funding to the EU, the UK presumably has a corresponding right to the benefit of EU payments – if the funding involves an accrued obligation on the UK, the payment presumably also involves an accrued obligation on the EU. But if the commitment is, for example, to the building of a road in an under-developed part of the EU, funding could be a one-way street so far as the UK is concerned.

The UK’s counter-argument is likely to be that any commitment to future funding is made by the EU, which has its own legal personality distinct from that of its member states (article 47 of the TEU, inserted by the Lisbon treaty of 2007). The EU’s member states are not liable for the EU’s obligations. Article 311 of the TFEU requires the EU to “provide itself with the means necessary to attain its objectives”, which the EU has done through the Council’s own resources decision. That decision requires payments to the EU by its member states, not by former member states that have ceased to be bound by the EU’s treaties.

But this, like many other questions surrounding Brexit, is territory that has not previously been traversed and for which there are no direct precedents. There is inevitably uncertainty.

The fact and amount of any post-Brexit payments by the UK to the EU will cause political controversy in the UK, and could also raise issues within the EU. If the UK refuses or is not obliged to fund EU commitments after departure, the EU will either have to raise additional revenue from the continuing member states, which will not be popular with the net contributors, or the EU will have to cut back its expenditure, which will not be popular with the net recipients.
Politics within the continuing EU could affect the tone and potential outcome

of negotiations with the UK – indeed, whether a deal is possible at all.

Timing

The process for setting the EU's budget for 2018 is due to start formally by 1 September 2017. Brexit should not in principle affect this annual cycle because the UK will probably remain a full member of the EU throughout 2018 (though the UK will be cautious about commitments stretching beyond March 2019).

The 2019 budgetary round should start by 1 September 2018 (though in practice it usually does so well before the deadline), when the UK will still be a member of the EU but the budget will be for a period largely after the UK's likely departure date. If agreement on the UK's financial obligations on withdrawal has not been reached by that time, the Commission will have to crystallise its position at that stage because the annual budget must include an estimate of the EU's revenue for 2019, including from the UK, and the EU's budget must balance. The EU's budget can be approved by qualified majority voting in the Council – so the UK cannot block it – but the mere inclusion in the budget of a payment from the UK as a result of withdrawal does not mean that the UK will in fact pay it or be obliged to do so.

Particular payment problems

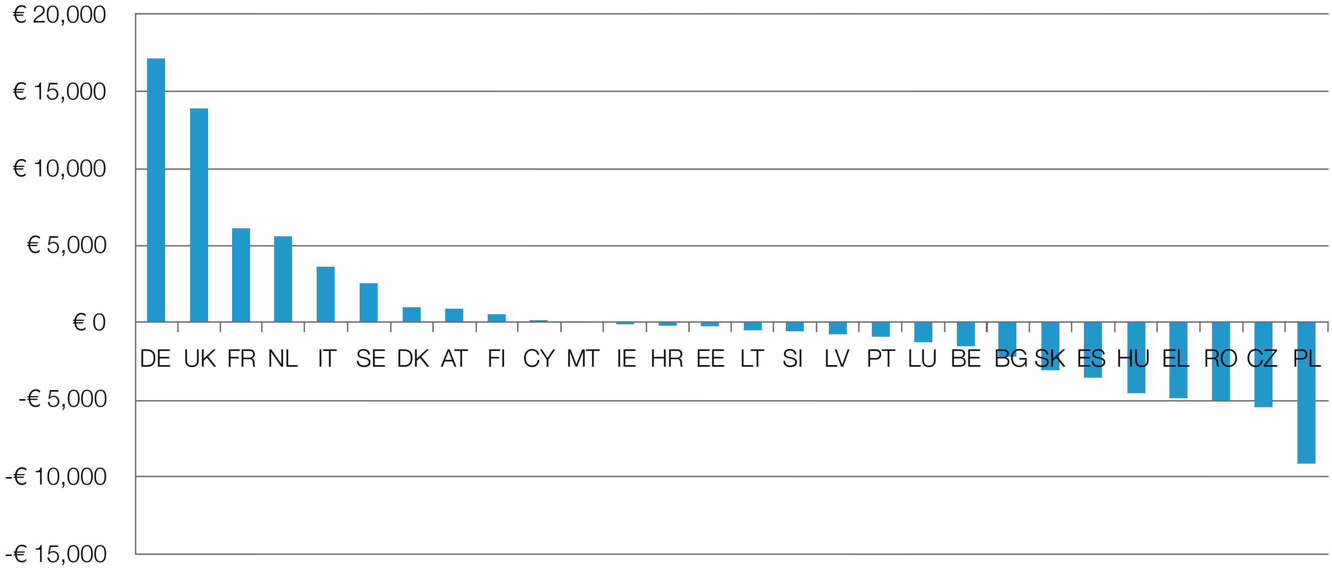
Even if it were possible for the UK and the EU to agree general principles, the application of those principles to the huge number of factual scenarios underlying the EU's complex financial arrangements could cause considerable complications and, with them, bring scope for negotiating friction, even breakdown.

To take a small number of further examples:

- The EU and its institutions have interests in real property, some of which will be held on long-term leases entailing legal commitments stretching over many years. Some of these leasehold properties are in the UK, such as the European Medicines Agency and the European Banking Authority, both of which are based at Canary Wharf in London. Should the UK pay its share of the future rent because the EU is legally obliged to pay it, even though the UK will not gain further direct benefit from the future work done at the properties (even assuming that the properties are retained)? What if the EU is able to realise or surrender a leasehold interest at a profit and to move into smaller premises that reflect the fact that the EU will, on the UK's withdrawal, have lost some 13% of its population and 16% of its income?
- If the EU or an EU agency is legally obliged to provide funding to a UK-based entity (eg a university or other research organisation) for a period that extends beyond Brexit day, the entity may be able to enforce that obligation against the EU despite Brexit, unless the terms of the EU's obligation provides otherwise. The fact that the obligation is owed to a UK entity should not make any difference if the entity has a legal right to payment. Equally, if this EU obligation generates a corresponding obligation on the UK to fund the EU that accrued prior to Brexit, the UK must pay, regardless of whether the research project is in the UK or elsewhere within the EU, because there is no allocation of UK payments into the EU's budget to payments by the EU to UK persons. But if there is no accrued funding obligation, the UK need not pay wherever the project is taking place.

Whatever the legal logic, forensically and politically it may be difficult to argue that the UK-based entities can continue to enforce rights to payment from the EU's budget but that the UK need not contribute to the budget that provides those payments. There may be the potential for a deal to be done, but the details will be tricky. For example, research projects often straddle borders, making allocation between the EU's member states more an art than a science.

The UK's Government's White Paper, *The United Kingdom's exit from and new partnership with the European*



Net EU revenue and expenditure by member state in 2015 (€ millions)
Source: European Commission, EU Budget 2015 Financial Report, Annex 2c

Union (February 2017), suggests a recognition of the need for a deal and also perhaps hints at a national approach. It says that all European Structural and Investment Funds projects signed before the UK's Autumn Statement in November 2016 "will be fully funded even when these projects continue beyond the UK's departure from the EU". The White Paper goes on that UK institutions should continue to apply for EU funding and that the UK "will work with the Commission to ensure payment when funds are awarded. HM Treasury will underwrite the payment of such awards, even when the specific projects continue beyond the UK's departure from the EU." The implication may be that post-Brexit funding will, if need be, come from the UK.

- The EU and its institutions have numerous employees who have accrued (and generous, by contemporary standards) pension entitlements. However, the EU has no pension fund into which pension contributions by employees are paid. Instead, employees' pension contributions are treated as income in the EU's budget (€527 million in the 2016 budget) and pension payments as expenditure (€1.647 billion in 2016). Employees' pension contributions should, actuarially, cover one-third of the pension cost, with the EU meeting the balance (article 83(2) of the EU's Staff Regulations, Regulation No 31 (EEC), dating from 1962). The cost of the EU's pension scheme as a whole is "charged to the budget of the Union. Member States shall jointly guarantee payment of such benefits in accordance with the scale laid down for the financing of such expenditure" (article 83(1)).

The EU therefore has an ongoing commitment to pay future pensions, and it might be argued that the UK should contribute its share for staff employed at EU institutions while the UK was an EU member state. Leaving aside the very considerable difficulties in calculating what the EU's pension aggregate liabilities are and how the UK's share should be assessed (the EU's balance sheet for the end of 2015 shows a non-current pension liability of €64 billion), the UK has benefited from the work of the EU's employees (eg in negotiating trade deals with third countries) and should arguably pay a price for that, including future pensions (though these could be very long term). The member states' guarantee set out in the Staff Regulations is, in itself, irrelevant since there is no suggestion that the EU will default on its pension obligations, even to UK nationals, but it might offer a basis for assessing the UK's accrued liability.

An alternative approach would for the UK to take on the EU's liability for the pensions of UK-domiciled or UK-resident EU employees and former employees. This may have a pragmatic attraction (especially to the UK, since the number of UK employees at the EU is disproportionately low), but perhaps less in legal logic. There is no national quota for EU officials, who are supposed to serve the EU and all its member states equally. The idea of national responsibility for EU employees may be difficult for the EU to accept.

- Many of the EU's obligations are contingent. For example, under the European Financial Stability Mechanism the EU borrowed in order to make loans to Portugal and Ireland. The EU must repay its loans, but in practice there could only be a liability on member states to contribute if the EU's borrowers default. Similarly, the common provisions regulation (Regulation 1303/2013/EU) covering the European Regional Development Fund, the European Social Fund, the Cohesion Fund and other similar EU funds includes EU support for financial instruments and for repayments to the EU. How should any liabilities be assessed, or can it be left on a wait and see basis?

These are just some of the scenarios that could arise. And even if it were to be agreed that the UK should make a payment for some accrued liabilities, the basis upon which that payment should be calculated is far from clear. It could, for example, be calculated on the basis of past gross contributions, past net contributions, GNI, population or some other basis.

The EU's assets

The EU and its agencies have many assets – from major items, like buildings and debts, to more trivial or granular items, such as the EU's wine cellar (reported in the press some years ago

European Union Balance Sheet, 31 December 2015 (€ millions)

Non-current assets		
Intangible assets	337	
Property, plant and equipment	8,700	
Investments accounted for using the equity method	497	
Financial assets	56,965	
Prefinancing	29,879	
Exchange receivables and non-exchange recoverables	870	**97,248**
Current assets		
Financial assets	9,907	
Pre-financing	15,277	
Exchange receivables and non-exchange recoverables	9,454	
Inventories	138	
Cash and cash equivalents	21,671	**55,448**
Total assets		**153,696**
Non-current liabilities		
Pension and other employee benefits	(63,814)	
Provisions	(1,716)	
Financial liabilities	(51,764)	**(117,293)**
Current liabilities		
Provisions	(314)	
Financial liabilities	(7,939)	
Payables	(32,191)	
Accrued charges and deferred income	(68,402)	**(108,486)**
Total liabilities		**(226,139)**
Net assets		**(72,442)**
Reserves	4,682	
Amounts to be called from Member States	(77,124)	
Net assets		**(72,442)**

Source: Consolidated Financial Accounts of the European Union, Financial Year 2015 at 42,500 bottles, split between the European Council and the Parliament) – all of which have been paid for by past contributions from member states. The EU's balance sheet as at the end of 2015 (COM(2016) 475 final) includes assets of €154 billion, 83% of which comprise loans, financial instruments, cash and pre-financing. The balance sheet also shows liabilities of €226 billion, with €77 billion of the shortfall to be called from member states in future annual budgets.

If the EU were to be dissolved, the benefit of these assets, after meeting the EU's liabilities, would be divided amongst the member states. The EU will, however, continue in existence after the UK's withdrawal, nor will that withdrawal affect the EU's legal personality or its title to its assets. It is not obvious that withdrawal would necessarily entitle the UK to a share of the EU's assets absent provision for that in the EU's treaties. On the other hand, if the EU were to demand that the UK continue with prior funding commitments (including any that generate assets for the EU), it might be argued that the UK should be entitled to the benefit of its past funding, though the manner of calculation will be anything but easy.

Certain EU-related assets may require special consideration. For example, the European Investment Bank was established under article 308 of the TFEU, which provides that the "members of the European Investment Bank shall be the Member States". When the UK leaves the EU, the UK will cease to be a member of the EIB. The EIB is not funded from the EU's general revenues but from its own capital provided by the member states. The EIB's total "subscribed capital" is €243.3 billion, of which €21.7 billion has been called, according to the EIB's balance sheet at the end of 2015. The UK's contribution to the EIB's called capital is €3.5 billion (or 16%).

The EIB's statutes do not contemplate a member state withdrawing from the EU and, as a result, ceasing to be a member of the EIB. The statutes are silent as to what should happen to a former member state's capital contribution on withdrawal. It seems unlikely that the UK's capital contribution could be forfeit, but it is a matter for negotiation as to how it can be returned and at what value (eg the amount paid or on the basis of the EIB's current asset value).

Dispute resolution

If the UK and the EU cannot reach agreement on who should pay what in respect of the UK's withdrawal, a means of dispute resolution will need to be found. The dispute should not be left to fester, potentially souring relations on other matters. What that means of dispute resolution should be is not easy to identify.

If, say, the EU or a member state decided before the UK has left the EU to take the matter to court, that court would probably be the Court of Justice of the European Union. The CJEU has jurisdiction over disputes concerning the interpretation of the EU's treaties (article 267 of the TFEU) – indeed, member states are not permitted to submit a dispute concerning the interpretation or application of the treaties to any method of settlement other than those provided by the treaties (article 344). A dispute over the terms of withdrawal is a dispute over the interpretation of the EU's treaties, even though it is largely a question of filling in the numerous gaps in article 50 of the TEU.

A reference to the CJEU before the UK's departure from the EU might be open to objections of prematurity or that it amounts to a request for legal advice rather than the resolution of a dispute. However, the CJEU has always jealously guarded its right to have the final say over the interpretation of the EU's treaties, effectively rejecting the first EEA Agreement and the EU's proposal to adhere to the European Convention on Human Rights because those new treaties would have infringed the CJEU's prerogatives in that regard (Opinions 1/92 and 2/13 respectively). The CJEU may not lightly relinquish its jurisdiction.

Even if the CJEU were to become seised of a dispute before the UK left the EU, that begs the question of whether the UK would continue to consider itself bound to participate in, and by the result of, the proceedings after the departure. The UK would no longer be a member state at that time and the EU's treaties would no longer apply to the UK.

After the UK has left the EU, the CJEU may arguably continue to have jurisdiction over the UK as regards the interpretation of the EU's treaties. In private law, jurisdiction clauses in contracts continue to apply notwithstanding the termination of the contract. It would not be surprising if the CJEU took that same view despite article 50(3) of the TEU providing that the treaties no longer apply to the UK.

The CJEU will be regarded by the UK as an uncongenial and, quite possibly, unacceptable forum, especially as UK's withdrawal from the EU will lead to the UK's Advocate General and judge leaving their posts at the Court (perhaps a reason why the CJEU's jurisdiction should be treated as ceasing on withdrawal). The UK Government's White Paper pledges to "bring an end to the jurisdiction of the CJEU in the UK"; the same may apply to the CJEU's jurisdiction over the UK. In the same paragraph of the White Paper, the Government says that the UK "will of course continue to honour our international commitments and follow international law", though it is questionable whether the UK would necessarily accept a decision by the CJEU on its own competence as definitive of the UK's obligations in international law.

If the UK does not accept the CJEU's jurisdiction, that would not stop the CJEU from deciding the case. If the CJEU were to decide that a sum was owed by the UK, there may be little the EU could do to enforce payment, but the decision would affect adversely future relations between the UK and EU.

Ideally another dispute resolution mechanism acceptable to both sides would be agreed (provided that the CJEU does not bar this by concluding that article 344 of the TFEU prevents the EU or its member states from agreeing to any alternative to the CJEU). The International Court of Justice at The Hague is not an obvious option because only states can be parties to cases before the Court (article 34(1) of the Statute of the ICJ), though a dispute could in theory be manufactured between one or more of the EU's member states on one side and the UK on the other. In general, the jurisdiction of the ICJ depends upon the parties agreeing to refer a dispute to the ICJ, but the UK has made a declaration under article 36(2) of the ICJ's Statute that it will, on a reciprocal basis, generally accept the jurisdiction of the ICJ. Certain other members of the EU (such as Belgium and Germany, but not France) have made comparable declarations.

More realistically, perhaps, an ad hoc tribunal might be required, but the nature of that tribunal will depend upon the nature of the disputes between the UK and the EU. If, for example, the dispute is as to whether one side or the other has any liability, that will be a question for international lawyers. But if the dispute is as to the quantification of pension liabilities, it may be that the tribunal should comprise, at least include, actuaries, whether as judges or assessors.

Conclusion

There is no precedent for what should happen to payments to the EU and to the EU's assets on a member state's departure from the EU. The UK and the EU must, to some extent, make it up as they go along, which offers flexibility but also considerable scope for disagreement. Deciding on the relevant principles is anything but easy. Applying those principles is extraordinarily difficult.

Post script

Since first publishing the above, the House of Lords Select Committee on the European Union has issued a report entitled *Brexit and the EU Budget* (March 2017). The Report illustrates the complexity of the EU's budgetary affairs and the huge difficulty in trying to fix upon any particular sum that the UK might be required to contribute to the EU on departure or vice versa. It also acknowledges the importance of reaching agreement as part of the process of establishing a satisfactory ongoing relationship between the EU and the UK.

Regarding the principle of whether the UK or the EU is obliged, legally, to pay anything to the other in the event that it proves impossible to reach a withdrawal agreement, the Committee received conflicting evidence. The Committee elected to follow the opinion of its legal adviser in concluding that, on balance:

- "No provision is made [in the TEU] for ensuring that EU obligations on the withdrawing state persist after the Treaties cease to apply"
- "Article 50 TEU allows the UK to leave the EU without being liable for outstanding financial obligations under the EU budget and related financial instruments"
- "Individual EU Member States may seek to bring a case against the UK for the payments of outstanding liabilities under the 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 of tribunal would have jurisdiction"
- "the UK will not be in a position, legally, to claim a share of the EU's assets upon withdrawal"

There are unquestionably difficult legal issues in determining whether and, if so, what the UK should pay the EU or the EU should pay the UK on the UK's withdrawal from the EU, but some elements in the reasoning adopted by the Committee may be open to question, including in respect of the following three areas.

First, the Committee notes that article 70 of the Vienna Convention sets out interpretative principles that apply "[u]less the treaty otherwise provides". The Committee concludes that because article 50 of the TEU addresses withdrawal from the EU, article 70 of the Vienna Convention has no application. This suggests that either the Vienna Convention or article 50 applies, but that there is no scope for both to do so. It is, however, arguable that it not necessarily one or the other. Where article 50 deals with a particular issue expressly, it clearly ousts the Convention; but where article 50 is silent or ambiguous, the Vienna Convention may remain relevant. The EU might be expected to follow general principles of international law or, where it does not wish to do so, to be clear that its intention is to depart from these norms. The Vienna Convention might only cease to be relevant to the extent that the TEU provides otherwise. Just because article 50 of the TEU occupies some of the ground regarding withdrawal does not automatically oust article 70 of the Convention in its entirety.

Secondly, the Committee takes the view that the UK's liability for sums unpaid and overdue at the date of the UK's withdrawal will be wiped from the books as a result of withdrawal. The basis for this view is that article 50(3) provides that the EU's "Treaties shall cease to apply" to a withdrawing state; the treaties created the payment obligation, which therefore disappears along with the treaties themselves. This approach perhaps gives insufficient weight to the full wording of article 50(3), which is that the "Treaties shall cease to apply to the State in question… from two years after the notification referred to in paragraph (2)". The treaties could cease to apply to the UK prospectively, but not retrospectively. If a sum fell due while the treaties applied to the UK, it might remain due even if new obligations cannot be created. This would be consistent with article 70 of the Vienna Convention (and normal principles in private law) rather than resulting in the possibly surprising conclusion that departure enables the UK to escape pre-Brexit payment obligations.

Thirdly, the Committee comments that other EU member states may seek redress against the UK for payment of outstanding liabilities. That is, of course, possible, but the UK's payment obligation, so far as it has one, will be to the EU itself, not to other member states. The natural plaintiff will be the EU. If the EU takes proceedings, it may do so in the CJEU (indeed, the CJEU could be the only forum in which, under the treaties, the EU is able to take proceedings). It is, perhaps, less clear than the Committee allows that the CJEU would cease to have jurisdiction, unattractive though continuing jurisdiction would be to the UK. Dispute resolution provisions generally survive termination of the underlying agreement, though there may be special circumstances rebutting that conclusion in this case. But the Committee is undoubtedly correct that enforcing any decision by the CJEU would be hard.

It is not necessary to follow the Committee in all the steps of its argument in order to conclude with it that there are serious legal issues regarding the payments, if any, due on the UK's departure from the EU. On the one hand, the UK can argue that: the EU is a legal entity distinct from its member states; any future payment commitments are the EU's, not its member states'; the member states' only obligation is to pay their annual dues under the treaties; and this payment obligation ends on withdrawal from the EU when the treaties cease to apply to the withdrawing state. On the other hand, the EU can argue that: EU finances involve commitments by member states to fund the EU over a period of years, not merely on an annual basis; those commitments involve an "obligation… created through the execution of the treaty prior to its termination" within the meaning of article 70 of the Vienna Convention; and those commitments therefore survive the UK's withdrawal from the EU.

What is beyond doubt is that the issue of payments on departure will best be resolved by negotiation rather than by litigation and that, as the Committee put it, what is involved is "more than a negotiation about withdrawal, and more than a trial of strength. It is also a negotiation about establishing a stable, cooperative and amicable relationship between the UK and the EU, so as to promote the security, safety and well-being of all the peoples of Europe. Such a relationship is inconceivable without good will."

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