COMMENTARY: HOW MONEY WILL DIVIDE EUROPE AFTER BREXIT

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Right now the European Union is united on one thing above all: to get Britain to pay as big a divorce bill as possible when it exits the EU. But while money will unite leaders at this weeks European summit, it will divide them after Brexit.

The British government once hoped that the Oct. 19-20 meeting would be the moment when the Brexit negotiations could move on to discuss trade. That aspiration now seems hopeless. European leaders look set to insist on further delay until there is more progress in the first stage of talks, above all in reaching agreement on how much Britain will have to pay to settle its obligations when it leaves.

Political discord at the heart of the British government and the weakness of Theresa May following the loss of the Conservative majority in the general election have undoubtedly been hampering negotiations. Not unreasonably, European leaders worry about striking a deal with someone who might not be prime minister when Britain leaves the EU in 17 months time.

The EU holds the strongest cards because what matters most for Britain is its future trading arrangements with the huge market on its doorstep. The deadline under the Article 50 withdrawal procedure increases the EUs leverage since Britain must leave with or without a deal in March 2019 (unless the 27 European states agree unanimously on an extension.) Despite hyped-up talk in London about preparing for no deal at all, Britain will do its utmost to avoid what would be a ruinous outcome, grounding flights to Europe and causing long hold-ups at border crossings, such as Dover on the south coast of England.

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If economic size and time favor the EU, the British governments strongest card is money - one that it has played in various guises for centuries with its continental neighbors - and it is naturally reluctant to show its full hand too early. Even so May has already made an important concession. As part of the transition period of around two years that she called for in her emollient Florence speech last month, Britain would continue to pay in to the EU budget to ensure that none of the member states was out of pocket owing to the decision to leave. These net payments of around □□□ billion ($11.8 billion) a year would fix the immediate problem facing the EU, the hole that would otherwise open up in its finances during the final two years of its current budgetary framework, which runs from 2014 to 2020.

But that extra money from aligning Britains effective date of departure with the end of the EUs budgeting plan will not be enough, for two reasons. One is the way the EU in effect borrows from the future, by making spending commitments that it pays for later. In principle, the EU cannot borrow to pay for expenditure. But, through its accounting procedures, the EU can and does commit it to spending that will be paid for by future receipts from the member states.

What this means is that even after 2020 there will still be payments due on commitments made under the current seven-year spending plan. That pile of unpaid bills, eloquently called the reste à liquider (the amount yet to be settled), is forecast to be □□□□ billion ($300 billion) at the end of 2020. Estimates of what Britain might owe towards this vary, but taking into account what might have been spent on British projects it could be around €20 billion ($23.6 billion).

On top of that □ and the second main reason why the EU is holding out for more □ the EU has liabilities, notably arising from the unfunded retirement benefits of European staff estimated at □□□ billion ($79 billion) at the end of 2016, which it is expecting Britain to share. Even taking into account some potential offsets from its share of assets, Britain may face a bill of between □□□ billion ($35 billion) and □□□ billion ($47 billion) on top of the □□□ billion ($23.6 billion) paid during the transition period.

Although money is Britains strongest card in the negotiations, there are political limits to the amount that the government can stump up. Brexit campaigners used inflated figures to exaggerate the money that could supposedly be switched into the health service from Britains contribution to the EU. That means the reality of having to pay a large exit bill could be electorally toxic. Yet in order to secure what really matters for Britain □ access on reasonable terms to the huge European market – Mays government will have to confront the public with this cost.

The British predicament is so extreme and rifts between Conservative ministers over how much ground to concede so acute that a breakdown in the negotiations is conceivable later this year. With so much attention focused on the political drama playing out in London, it is easy to lose sight of the fact that the EU will face a harsh budgetary future even with a substantial divorce settlement. Indeed the insistence that Britain pay up is a sign of the strains that will come to the fore after the transition period ends. The EU will lose one of its big net contributors, the second largest after Germany in 2015.

The EUs budget of around 1 percent of GDP is in any case puny given the scale of its ambitions. Those hoping for greater generosity on the part of the remaining rich countries are likely to be disappointed. With German Chancellor Angela Merkel weakened following her poor performance in the federal election, Germany will be even more tight-fisted than before in its efforts to avoid anything that smacks even faintly of a transfer union. Yet if the poorer countries receive less, that will sharpen the north-south divide that emerged so starkly during the euro crisis when countries such as Finland resented having to contribute to bailouts — especially to Greece — while southern states smarted at the imposition of austerity. And it will exacerbate tensions with eastern countries such as Poland that are big beneficiaries from the EU budget.

Both Jean-Claude Juncker, president of the European Commission, and — more important — French President Emmanuel Macron, have recently set out plans to reboot Europe. But these grand visions will count for little unless they are matched by the solidarity of hard cash. At present the EU can make common cause in pursuit of Britains exit bill. But once Britain leaves, the bickering over money will begin – and the push toward a stronger union could be tougher than ever to achieve.

About the Author

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