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False assumptions underpinned British strategy

By Alex Barker and George Parker

UK's isolation at EU summit follows policy of secrecy



Nicolas Sarkozy (left) and David Cameron at the December 9 summit in Brussels

Statecraft in Europe is usually exercised on a full stomach. So it was that Angela Merkel and David Cameron sat in the stark white dining room of Berlin's chancellery on a cold November afternoon, picking over roast duck and plotting an Anglo-German trade-off that would reshape the European Union.

It was to be a fateful discussion about a potentially toxic subject. The German chancellor was determined to lash down wayward eurozone countries in strict fiscal rules to be enshrined in a new EU treaty. At a time of panic in the markets, her zeal for difficult, long-term treaty change was unsettling her partners.

Treaty change presented big political problems for the UK prime minister, with eurosceptic rebels in Mr Cameron's Conservative party ready to seize on any opportunity to force a referendum on Britain's membership of the 27-nation EU.

But the prime minister expressed understanding for Ms Merkel's game plan. She found British politics "incomprehensible" but promised she was ready to look for "sweeteners" that might make a deal in Brussels acceptable to the Tory backbenches. "Tell me what you want and I will find a way," she said, according to a note of the meeting.

One big question remained. "What about France?" asked Mr Cameron, fearing President Nicolas Sarkozy would scupper any UK concessions. Ms Merkel, Europe's reluctant paymaster, calmly looked up: "Nicolas will agree."

With those words a high-stakes "Berlin-first" diplomatic strategy was born, a British gamble with potentially momentous consequences. European leaders had long grown accustomed to Ms Merkel's cautious diplomatic style and her tendency to wait until the last minute to show her hand. But Mr Cameron left Berlin convinced she was fixed on full treaty change at 27, seemingly whatever the obstacles, and whatever the British price. In Downing Street the view was that there was a "G1 in the eurozone" – Germany – and it would prevail.

German officials did not quite see it that way. They say that, while this was a "yes we can" meeting, Mr Cameron did not mention that he might be asking for treaty changes to protect UK financial services. Ms Merkel was clear that she did not want to open a Pandora's box of concessions for a string of other member states. There were limits to what Ms Merkel would pay. A Plan B was prepared, should treaty change prove too costly.

Weeks later, at a summit in Brussels, the false assumptions underpinning the British strategy would be brutally exposed, in a defining night of diplomacy played out against the menacing backdrop of the sovereign debt crisis. Following numerous interviews with participants, the Financial Times has pieced together what happened in those two weeks.

Safeguards and secret preparations

In the early hours of Friday December 9, Mr Cameron defiantly vetoed proposed EU treaty changes because they did not contain his required "safeguards" for the City of London. Conservative eurosceptics and most UK voters were delighted. Ms Merkel "jumped late", as the British predicted. But she sided with the French. As dawn broke over Brussels, Britain stood alone, as 26 member states peeled off to form a pact outside the EU treaties. "The biggest mistake was thinking they could divide the Franco-German axis on the euro," says one senior EU official. "Heaven knows they have differences, big differences. But you exploit their divisions over the euro at your peril."

To some, the UK miscalculation came in pushing on treaty change for the City of London – a protocol allowing the City to snatch back power for national regulators – and failing to sell this to its allies. When Ms Merkel offered help, she was largely in the dark about what Mr Cameron wanted. For most of Britain's allies, and even its own most senior diplomats, the secrecy would remain until the eve of the summit. "When we talked to the Brits just the day before, we thought they were seriously looking for a solution for this mess," says a senior Nordic official. "When we saw their list, our experts said: 'They're not serious. It's just too much.'"

Some unnamed Whitehall figures have blamed Sir Jon Cunliffe, Mr Cameron's summit "sherpa" and soon-to-be ambassador to the EU, for failing to prepare the ground. But in reality it was Mr Cameron and William Hague, the UK foreign secretary, who decided on tactics.

They wanted the bid to be kept secret from two potential adversaries. The first was Mr Cameron's hardline eurosceptics, who want an EU referendum and repatriation of powers. If details of Britain's rather technical demands covering arcane aspects of City regulation had reached the Tory benches, Mr Cameron could have arrived in Brussels with a mutiny raging at Westminster. The second was France, for fear that as the demands were circulated, Paris would seize on them and use them to discredit Britain's position, claiming Mr Cameron was trying to protect the villains of the financial crisis at the expense of the eurozone.

Moreover, the British position was not settled till late. On Tuesday December 6, Mr Cameron assembled his chief foreign policy advisers. Mr Hague, whose euroscepticism defined his own leadership of the Tory party a decade ago, pressed for repatriation of powers. Sir Jon said there was leverage to extract concrete concessions, short of an opt-out. Ed Llewellyn, Mr Cameron's chief of staff and an old Brussels hand, warned of the dangers of pushing too hard.

Shopping lists, existential issues

Mr Cameron opted to trim his demands. Looser EU labour laws and an "emergency brake" on all financial regulation were scratched off the shopping list – evidence that he was not set on a wrecking strategy. But crucially, he would insist his concessions were written into the treaty. Nick Clegg, Mr Cameron's deputy and Liberal Democrat coalition partner, gave his seal of approval.

It is unclear whether Mr Cameron was aware of the warning lights flashing in the Whitehall machine. Most striking was the reporting from Simon McDonald, Britain's ambassador in Berlin. His dispatch warned that the chancellor thought Britain was overbidding; she was not wedded to treaty change at all costs. One

senior British official describes the dispatch as “millimetre perfect” in its judgment.

From Paris, too, came warnings that Mr Sarkozy was intent on a weaker, intergovernmental pact. Others in Whitehall said a breakaway pact would quickly snowball to cover most EU members. “Every dog in the street knew it was going to be more than 17,” says one senior EU official. José Manuel Barroso, the anglophile president of the European Commission, its executive arm, pleaded with Mr Cameron to “keep it reasonable” or risk fragmenting the union.

Berlin, meanwhile, was warning London not to overdo it in pushing Germany. Nikolaus Meyer-Landrut, Ms Merkel’s Europe adviser, was given early sight of the City protocol and said it went too far. When asked what was acceptable, German officials made clear it was not their place to draft UK demands. After a flurry of Franco-German diplomacy, a common position took shape: if the British did not temper their demands, a deal would be done without them. Days before the summit, German officials said their “pessimism was more pronounced” – words intended as a clear signal to London.

When did Ms Merkel give up on Mr Cameron? The exact point is unclear. Senior European and British officials believe it was at the European People’s party summit – a gathering of all the main centre-right leaders in Europe – in Marseilles on the morning of December 8, just hours before the EU summit began in Brussels.

Ms Merkel met Mr Sarkozy in the French port city. The two have never forgotten Mr Cameron’s decision – unveiled when he became Tory leader in 2005 and realised four years later – to take his party out of the EPP, much to their anger. According to a European official in attendance, Ms Merkel’s shift was evident behind closed doors. She said an intergovernmental treaty remained her Plan B, but it now appeared the most likely outcome.

At 7.30 that evening, the British, French and German leaders crammed into a small French delegation room overlooking a giant air vent on the roof of the Brussels Council building. The British had no reliable intelligence from the Marseilles meeting and nobody from Paris or Berlin had tipped off Downing Street about what was going on; Mr Cameron was in effect ambushed.

Flanked by Mr Hague, the prime minister watched stony-faced as the German chancellor said: “This is terrible – this is an existential issue for us. We can’t go your way.” She told him an exemption for the industry that caused the financial crisis was politically impossible.

Contradictions or nuances

It was 2am before Mr Cameron finally made his pitch to the summit. By then, the leaders had discussed details of the fiscal pact for five hours; most of them were already tired.

Mr Cameron cast his safeguards as minor tweaks. One witness says he stopped short of outlining the entire financial protocol. Most leaders were either baffled or alarmed by the attempt to reverse majority voting in certain areas. Some spoke out.

Mr Sarkozy was characteristically blunt. “David, we will not pay you to save the euro,” he said, according to one account. He went on to rebuke Helle Thorning-Schmidt, the freshly elected Danish prime minister, for the temerity to speak up for a deal at 27. “You’re an out, a small out, and you’re new. We don’t want to hear from you,” Mr Sarkozy said.

At this crucial point, Mr Cameron stopped using the BlackBerry with which he had been communicating with advisers. His team outside was cut off. An offer was made, initiated by Mr Barroso, to insert treaty language to protect the EU single market. Mr Cameron would not budge, readying for tough negotiation.

After little more than 20 minutes, a veto declaration came, not from Mr Cameron but from Herman Van Rompuy, the Belgian who as president of the European Council chaired the session. There was no vote. With little warning, Mr Van Rompuy closed the discussion of treaty change at 27, saying the UK could not be accommodated. That angered some British officials. “He ducked it and chickened out and made a sprint to a finish line that no one wanted to finish at,” one says.

Following a short break, Mr Cameron played his final card: refusing to let EU institutions support an intergovernmental treaty. His bargaining position relied on Hubert Legal, the aptly named head of the Council legal service. At a summit preparatory meeting, Mr Legal’s advice stressed the constraints on a pact outside the EU treaties. But his advice to the summit had a different emphasis.

Two ambassadors in Brussels insist Mr Legal’s views were not contradictory, merely nuanced. A senior EU official at both meetings says Mr Legal “did not [change his] mind at all”. But British officials are unconvinced. “We thought they would get another lawyer – in the end they didn’t need one,” says one. Another adds: “You could say he did a couple of triple somersaults and a double Salchow [a jump in ice-skating] and came up with the opposite view.”

Mr Sarkozy was adamant the deal had to be settled before markets opened. There was a scramble to agree a communiqué – detailing potentially fundamental changes

to fiscal sovereignty – in the middle of the night under absurd time pressure. “You can’t imagine the chaos,” says one who was there.

Unsettled bills and diplomatic costs

The eurozone then produced a statement committing EU members to providing €200bn (\$260bn) of assistance to the International Monetary Fund to tackle the crisis, even though nobody had any idea how the bill would be divided or whether all 27 member states were prepared to pay.

Those in attendance say Mr Cameron emerged as chirpy as ever, even when sharing a tiny lift with Ms Merkel. A French official casts the outcome as almost inevitable, given Mr Cameron’s bid. “We were not very surprised,” says one senior official. “There was no aggression, no animosity, no regret either. It is a domestic political constraint in the UK ... What can one do?”

One British official at the summit says there was little alternative by that point.

“When the lights come up and you realise there is a big Franco-German wall in front of you, it is very hard to change course.”

Downing Street insiders admit British interests in Brussels have been damaged – as Mr Clegg has warned. But they say that Mr Cameron ran a bigger risk – and faced a bigger clash with Europe – if he came back from Brussels with a deal that was later wrecked in the House of Commons.

Even committed europhiles in the government admit the outcome may not be as bleak as they feared. Diplomats are still scrambling to pin down basic details of the pact, ranging from what the pact covers to whom it applies to. “It is a bugger’s muddle,” says one. Several countries face political problems over ratification. Old allies are expressing second thoughts about leaving Britain in the lurch.

Points of leverage remain – particularly over the role of EU institutions in enforcing any treaty – and Britain could still be part of a deal to “integrate” the pact into existing treaties.

“This is a deal no one likes, not even the French,” says one senior diplomat in Brussels. “I have never felt a more depressed atmosphere. People are saying: what have we done?”

THREE SOLUTIONS TO ONE CRISIS

When the leaders of the 27 European Union member states gathered in Brussels this month,

their meeting was billed – not for the first time – as a “summit to save the euro”.

The main topic was a treaty to instil long-term fiscal discipline in the crisis-ridden eurozone – a German initiative to ensure the taxpayers of Europe’s richest country that they would never again have to bail out profligate states.

The deal involved much closer fiscal integration and semi-automatic sanctions to enforce budget discipline.

There were three main options for implementation, which split opinion across the bloc.

Berlin preferred full treaty change, which involves reopening existing EU agreements. This has the strongest legal weight. But it is fraught with political difficulties and triggers referendums in some states.

Another way forward is to go outside the EU treaty with an intergovernmental pact. This uses a narrower legal base and there are restrictions on EU institutions enforcing the rules. Some states still face ratification difficulties.

The third option, backed by the European Commission, involves using existing treaties to make room for a new pact. This was ruled out by Germany, but is popular with smaller countries.

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