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When Some Are More Equal than Others: National Parliaments and Intergovernmental Bailout Negotiations in the Eurozone

This article argues that the integration of financial assistance capacity in the eurozone, which was meant to remedy institutional shortcomings and mitigate the distributional implications of financial support in the European Monetary Union (EMU), has instead contributed to a deepening of the existing political cleavages and the creation new ones. This dysfunctional effect reflects the empowerment of *some* national parliaments in decisions on financial assistance. These arguments are tested against the empirical examination of the negotiations of the three adjustment programmes for Greece. Specifically, the article shows that negotiations moved towards the radicalization of creditors' positions and increased divisions between creditors in conjunction with the integration of financial assistance capacity. While advancing its theses, the article strikes a note of caution regarding the argument that the empowerment of national parliaments in EU policymaking is one of the most powerful antidotes to its legitimacy deficit and thus a safeguard for the integration project.

Keywords: EMU, financial assistance, national parliaments, intergovernmental negotiations, Greece, ESM.

Since the beginning of the sovereign debt crisis, eurozone policymakers have been forced to address a rather unfamiliar need: financial assistance for member countries.[1] This exigency has challenged the EMU in an unprecedented manner. First, it has exposed the institutional limits of the monetary union (Baldwin and Giavazzi 2016; Matthijs and Blyth 2015). When the crisis started, no institutional framework was in place for managing sovereign liquidity crises and reducing the risks of contagion.[2] The need to extend assistance to member countries in financial distress has also challenged the strength of European solidarity (Jones 2012). Specifically, it showcased the distributional implications that arise from channelling resources to countries in need from those countries with stronger financial positions.

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Eurozone policymakers have addressed these challenges through the progressive development of a regional financial assistance framework. That is, member countries have deepened their integration by designing a set of mechanisms through which the European Monetary Union (EMU) is now expected to address confidence crises stemming from imbalances in individual countries and spillover effects (ECB 2011: 73-4). As will be reviewed at greater length below, this integration progress culminated with the creation of the European Stability Mechanism (ESM) in 2012.

This article argues that this further step in the integration process, which was meant to remedy the institutional shortcomings of the EMU and mitigate the distributional implications of financial assistance, has instead contributed to the deepening of existing political cleavages (between creditor and debtor countries) and the creation of new ones (among creditors). The radicalization of intergovernmental negotiation has less to do with the incompleteness of European Union (EU) integration (Jones, Kelemen and Meunier 2016) and more to do with a specific set of 'political dysfunctions' of the kind examined in this special issue. Specifically, the article argues and illustrates that the empowerment of *some* national parliaments in the process through which financial assistance is decided and disbursed is a crucial contributor to the deterioration in the negotiation dynamics among member states.[3]

Involving national parliaments in decision-making regarding financial assistance changes the negotiation dynamics in two important respects. On the one hand, as the logic of the two-level game suggests (Putnam 1988), negotiating in the shadow of domestic constraints makes compromise more difficult for governments whose parliaments have to approve the lending scheme. This, in turn, is likely to affect the negotiation process by creating incentives for brinkmanship. On the other hand, the involvement of national parliaments in intergovernmental decisions alters the nature of policy coordination among member governments. Specifically, since governments have to win the support of national legislatures, the incentives to accommodate differences and identify with each other's problems become less influential than under conditions of intergovernmental deliberations (Bickerton, Hodson and Puetter 2015; Puetter 2012, 2014).

The article applies these theoretical arguments to the negotiations surrounding decisions on the three adjustment programmes for Greece. The Greek negotiations offer an almost natural laboratory to assess the impact of the integration of financial assistance capacity in the eurozone. Whereas under the first two programmes financial assistance was delivered through ad hoc, temporary mechanisms within the Troika framework,[4] the third programme was administered only through the ESM. Using a systematic analysis of the financial press and interviews with top officials involved in drafting the terms of the adjustment program,[5] this article shows that the dynamics of the negotiation changed over time. Specifically, negotiations under the ESM were characterized by the radicalization of creditors' position and increased divisions in the creditors' camp.

Of the creditor countries, the article focuses in particular on the German government's position. Germany played a central role in the management of the eurozone crisis (Bulmer 2014), and the German Bundestag is one of the national parliaments whose powers have significantly increased since 2010 (Auel and Höing 2014). Furthermore, for the purposes of this analysis, the Bundestag is the only parliament that has to vote both ex ante and ex post on lending programmes under the ESM (as explained below). Analysing the evolution of the German government's position in light of the changing powers assigned to the Bundestag in the bailout negotiations thus sheds a unique spotlight on the effects of national parliaments' involvement on intergovernmental negotiations at the EU level.

In order to control for alternative factors that might have influenced the German government position in the bailout negotiations, the article leverages as much as possible on the comparative method and the use of counterfactuals. In particular, it relies on the cross-time comparison of the three negotiation rounds and on selected cross-country comparisons. The purpose of the cross-time comparison is to exclude the possibility that the German position was solely influenced by the government's preferences for fiscal consolidation rather than by a combination of these preferences and the constraints exerted by the domestic legislature. If the government's preferences were the only driver of the negotiating stance, we would expect to see a radicalization in the negotiating stance when confronted with deviations from the fiscal targets by the Greek authorities. However, as the empirical analysis is going to show, even if the first programme went off-track and the commitment to fiscal discipline by the Greek government was uncertain, the German government conceded to new financial assistance in 2012 under a programme that even contemplated a temporary relaxation in the fiscal conditions. Furthermore, an excessive emphasis on the German government's preferences risks obscuring important differences of views within the government and cannot thoroughly explain the varying influence of cabinet members on the chancellor's negotiating stance (as discussed below).

In addition to the cross-time comparison, the article relies on selected comparisons between the German stance and that of other creditor countries. Specifically, the article compares the German negotiating stance with that of the governments most closely aligned with Germany on the bailout negotiations but with weaker levels of empowerment of national parliaments, as is the case for Finland. The purpose of this focused comparison is to try to isolate the causal influence of the institutional context on the dynamics of the negotiations regarding Greece.

The analysis conducted here contributes to scholarly and public debate on the modalities that close EMU legitimacy deficits and strengthen the integration process. Specifically, the article signals the risks to eurozone integration that stem from the elevated involvement of national parliaments in distributive issues at the EU level – among which financial assistance decisions certainly stand out. To be clear, the study does not deny the important role that national parliaments can play in rendering EU policymaking more responsive and accountable to the citizens of the member states (Bellamy and Kröger 2016; Bellamy and Weale 2015). That is, it is not one of the purposes of the article to suggest that the Lisbon agenda to strengthen parliaments' role in EU decision-making should be scrapped. However, while the post-Lisbon involvement of national parliaments with EU policymaking was primarily a means to bring EU affairs to the domestic level to legitimize them (e.g., Cooper 2012), national parliaments' involvement with ESM policymaking has led to the paradoxical situation where it is not EU policy that is 'domesticated' but (some) domestic politics are elevated to EU-level policy.

Before proceeding, some clarifications are in order as to the scope of the analysis. The article examines the implications of the institutionalization of the EU crisis management framework on the creditors' side. In this light, the article complements studies that have focused on the Greek negotiating position (Featherstone 2011; Tsebelis 2016) and on the politicization of EU economic governance in the domestic politics of member states since the start of the sovereign debt crisis (Leupold 2016; Roth, Jonung and Nowak-Lehmann 2015). Given the focus on intergovernmental negotiations, the study does not investigate the determinants of national parliaments' positions towards Greece and financial assistance in general. Finally, as will be further clarified in the next section, the analysis focuses on parliaments' involvement in the application (execution) of ESM treaty measures, not on parliaments' involvement in the ratification of the treaty. In other words, I focus on the 'ordinary' decisions that stem from the entering the intergovernmental treaty.

The article proceeds in three steps. The next section brings together two strands of literature that have flourished with the onset of the crisis but that have not been systematically engaged with each other thus far – namely, the literature of the involvement of national parliaments in the EU integration process and studies on intergovernmental decision-making. The second section examines the evolution of the EU crisis management system from the start of the sovereign debt crisis to the creation of the ESM. The third section provides empirical support for the proposition that the ESM contributed to deepening and expanding intra-EMU tensions.

THE IMPACT OF NATIONAL PARLIAMENTS ON THE DYNAMICS OF INTERGOVERNMENTAL NEGOTIATIONS

The sovereign debt crisis has sparked renewed interest in the impact of EU integration on the domestic politics of member states. In particular, increasing attention has been devoted to investigating national parliaments' involvement in the EU integration process (see the contributions in Auel and Höing 2014; Bellamy and Kroger 2016; also Winzen 2012). This literature has been focused on explaining how national parliaments have framed EU integration and exerted control over national governments for decisions regarding integration at a time of unusual politicization (Kriesi and Grande 2014; see also Hooghe and Marks 2009) and polarization as radical populist right and left parties voice strong opposition to EU politics (De Vries and Edwards 2009).

Along with renewed interest in domestic politics, the crisis has also sparked renewed interest in intergovernmental decision-making. Crisis management efforts have been pivotal in this regard as the European Council and the European Economic and Financial Affairs Council (ECOFIN) have taken the lead in coordinating policy. In one calculation, for instance, the European Council, which is expected to meet 'twice every six months' (TEU Article 15.3), met nine times in 2011, six times in 2012, six times in 2013 and six times in 2014.[6] In short, the European Council has become 'the centre of political gravity' in Europe (Puetter 2012: 161). This conclusion is reinforced by the weakening of domestic and supranational institutions in the EU decision-making process. For instance, Sergio Fabbrini (2015: 145) notes that 'national parliaments … had very limited impact on intergovernmental decision-making' during the crisis. At the same time, several scholars have identified a progressive erosion of the Commission's power of initiative as a driver of EU integration (Hodson 2013) and the European Parliament's ability to act as a check on the European Council and euro group decisions. In a scathing analysis, Vivien A. Schmidt (2015: 18), for example, notes that 'The EP has been sidelined in Eurozone governance, leaving it little formal legislative role in Eurozone policy formulation, which is mainly the domain of the Council, and little formal control over the Commission in the European Semester, let alone over the "Troika".'

This study brings together the two strands of literature discussed thus far – the literature of the involvement of national parliaments in the EU integration process and the literature on intergovernmental decision-making. Specifically, the article explores the implications of national parliaments' involvement for the dynamic of intergovernmental negotiations. Little research thus far has investigated this relationship beyond an examination of the indirect control mechanisms that national parliments exert on governments (Winzen 2012). Liberal intergovernmentalist works on the management of the euro crisis have come closest to discovering the connection between the involvement of domestic actors in intergovernmental negotiations (Schimmelfennig 2015). However, in keeping with the focus of this research tradition – according to which the relevant domestic actors and interests vary by issue area – significant attention has been placed on the influence of business and government preferences rather than on the influence exerted by national parliaments (Schimmelfennig 2015: 180)

In the following, I specify how national parliaments' involvement in the making of decisions regarding EU integration can affect the intergovernmental bargaining process. In doing so, I build on the literature on how domestic factors affect international negotiations. Since Putnam's powerful metaphor of the two-level game (Putnam 1988), the relevance of domestic ratification constraints for international negotiation outcomes has been extensively ascertained and investigated. These constraints, which include the 'interplay of institutional requirements necessary to ratify an international treaty' (Hug and König 2001, 453), are important to international negotiations because they hinge on the negotiators' room for manoeuvre in formulating a negotiating position and accepting a deal. The logic here is the negotiating stance reflects not only the negotiators' own preferences but also those of the relevant domestic ratification actors. In other words, negotiators anticipate the reaction of the domestic actors that have to ratify the international treaty, adjusting the negotiating stance in a manner that allows the exaction an acceptable deal for those actors. To use Putnam's language, the 'win-set' of the negotiator is influenced by domestic actors' preferences and institutions (Putnam 1988, 442-450). Although significant differences of view exist as to what domestic configuration provides international negotiators with more bargaining power over others,[7] the importance of domestic factors for the outcome of international negotiations is rarely called into question.

This article builds on this research tradition but also shifts the focus away from the outcome of the negotiations to their process. Specifically, I propose two expectations regarding the ways in which the involvement of national parliaments is likely to affect the dynamic of intergovernmental negotiations in the EU. The first expectation relates to the intensity of the political cleavages during the negotiations. Previous studies have shown that intergovernmental negotiations are characterized by definition 'by hard bargaining and brinkmanship' (Schimmelfennig 2015: 185). However, the extent of brinkmanship is far from static, otherwise it would be difficult to account for why some intergovernmental bargains are concluded quite quickly and others require extremely lengthy negotiations (Tsebelis and Hahm 2014). Hence, it is plausible to expect brinkmanship to vary according to the domestic constraints that governments face when negotiating with their peers. The implication of this proposition is testable. Specifically, we should expect to see increased brinkmanship across time and in conjunction with the increased involvement of national parliaments, whose approval of international deals represents one of the tightest constraints a government faces in supranational negotiations.[8]

The second expectation relates to the number of political cleavages that become relevant during the negotiations. Specifically, I expect that national parliaments' involvement is associated with an increase in the number of rifts. As a former European Central Bank (ECB) member observes, 'The explicit involvement of national parliaments, especially in Germany, gives the impression that it is ultimately up to the latter to agree on whether another Eurozone country can access the ESM and receive financial assistance. This creates a direct opposition between countries … which is very detrimental to the process of political integration' (Bini Smaghi 2015, 761). In other words, the expectation is that the incorporation of national parliaments in decisions related to financial assistance increases the likelihood of, and the motivations for, disagreement among member states. For this proposition to hold, the empirical analysis should find a repositioning in member states' negotiating stance over time – in particular, a repositioning among previously aligned governments as a function of the modalities of national parliaments' involvement.

CRISIS MANAGEMENT AND FINANCIAL ASSISTANCE IN THE EUROZONE

The theory of how to stem financial instability is well established at the domestic level. It revolves around the notion of the lender of last resort (LoLR) – a role usually assigned to the central bank. [9] In providing emergency liquidity assistance to banks that are solvent but illiquid, the central bank can prevent panic-driven bank runs, the fire sales of assets and a breakdown in the credit system; any one of these circumstances can create a chain of events that can have significant negative macroeconomic consequences.[10]

On the heels of the integration of global capital markets and in light of the experience of the crises in the emerging markets in the 1990s, increasing attention has been paid to the issue of the need for an international LoLR for sovereign states (Fischer 1999; Giannini 1999).[11] In this debate, attention inevitably focused on the International Monetary Fund (IMF). Indeed, the IMF has long performed the role of crisis manager for its members (Boughton 2000). Specifically, the Fund has contributed to curbing panic in sovereign debt markets by providing financial assistance to countries that are not able to finance themselves at a sustainable rate.

In addition to the IMF, several regional financing arrangements exist whose purpose is to provide financial assistance to countries in difficulties, drawing resources pooled or committed at the regional level (for a review, see IMF 2013). Among these, the system that was developed in the eurozone after the start of the crisis provides one of the most recent examples. Initially, this system was based on a temporary crisis resolution mechanism: the European Financial Stability Facility (EFSF).[12] Confronted with continued financial turbulence, euro area authorities eventually boosted the profile of their crisis management framework, creating the permanent ESM as of mid-2013 (see Gocaj and Meunier 2013; Schwarzer 2015).

According to the founding Treaty, the ESM is responsible for providing temporary financial assistance packages to euro area member states under strict conditionality.[13] Specifically, financial assistance is linked to the implementation of economic measures specified in a memorandum of understanding between the member state and the European Commission, which acts as the negotiating agent for the ESM and monitors programme implementation. The ESM's main decision-making body is the Board of Governors, consisting of the finance ministers of each ESM member, as well as the European Commissioner for Economic and Monetary Affairs and the ECB president as observers.

The decision to grant stability support to an ESM member is usually taken by the Board of Governors through mutual agreement.[14] As the ESM (2015a) itself clarifies, mutual agreement entails that 'the decision will be adopted only if all Governors vote in favour of the decision or abstain'. In deciding on ESM activities, members of the Board of Governors are subject to national procedures. These apply to both the decision to grant, 'in principle', stability support (for example, the decision to grant the Commission the mandate to negotiate a memorandum of understanding) and the approval of the outcome of the negotiations with the country that requests financial assistance (ESM 2015b). National procedures may entail approval from the government but might also require parliamentary consultation or even a parliamentary vote, which would be the most demanding requirement.

Looking into the national procedures of euro area countries, the national parliament of only one country – Germany – is involved in approving stability support both ex ante (on the decision to start the negotiations between the ESM and the member country seeking financial assistance) and ex post (on the outcome of the negotiations). This power derives from a national constitutional choice. Specifically, a series of judgements were issued by the German Constitutional Court following the start of the sovereign debt crisis through which the court specified the conditions under which Bundestag authorization is required to safeguard the parliament's budgetary responsibility (see, e.g., Höing 2012). In other countries, legislatures vote either ex ante (for instance Austria) or ex post (Estonia, the Netherlands and Spain) in their plenary format – or are not required to vote at all.[15] Among the creditor countries most closely aligned to Germany in their 'hawkish' stance towards Greece, it is worth noting that Finland's decisions pertaining to ESM loans are subject to the scrutiny of a parliamentary committee and not of a plenary session (for an overview of the different modalities of national parliaments' involvement, see Kreilinger 2015).

FROM THE FIRST TO THE THIRD ADJUSTMENT PROGRAMME FOR GREECE

The Greek crisis provides a natural case study to ascertain the effects of the integration of financial assistance capacity on the political cleavages among member states. Indeed, the negotiations for providing Greece with financial support proceeded in parallel to (and were often a major driver of) the development of the new crisis management system. This is well reflected in the modalities through which financial assistance was disbursed in the three adjustment programmes, with only the last programme covered entirely through the ESM.[16]

In the following, I trace the negotiations of the Greek adjustment programmes showing the progressive stiffening of creditors' positions towards Greece and growing divisions among creditor countries.

The Beginning: The First and the Second Adjustment Programmes

Greek economic problems can be traced back to the period following the country's accession to the eurozone. Because of declining borrowing costs, the country's fiscal position deteriorated as public spending increased, especially spending in social transfers and pension benefits. Aside from the deterioration in the fiscal balance, the upward trend in relative wages and prices had undermined Greek competitiveness, creating a very large current account deficit.

When the newly elected Papandreou government revealed in October 2009 that the budget deficit would amount to 12.5 per cent of GDP, more than twice that previously reported, Greece's problems appeared quite small from a systemic perspective – Greece represents approximately 2 per cent of the eurozone's GDP. Given its level of financial integration into the eurozone, however, Greece's problems shook the stability of the monetary union and required substantial international support.

This support materialized in the form of conditional financial assistance negotiated with the Troika in May 2010. Specifically, the eurogroup agreed to provide bilateral loans pooled by the European Commission through an ad hoc facility for a total of €80 billion, which was to be disbursed over the period of May 2010 through June 2013. The financial assistance supported by eurozone member states was part of a joint package that included a €30 billion IMF loan. As for its content, the programme pursued a twofold strategy. First, it aimed at bringing domestic demand in line with domestic supply capacity through a substantial fiscal adjustment on the order of 11 per cent of GDP during 2010–13 in addition to the 5 per cent of GDP in measures adopted in 2010. Second, the programme aimed at improving competitiveness through the implementation of structural reforms. The focus was on streamlining public administration and liberalizing Greece's rigid labour markets to set the stage for long-term economic growth.[17]

By the summer of 2011, however, it became clear that all major economic projections were off track; GDP had contracted more than expected and public debt as a share of GDP continued to rise (IMF 2011: 66). Competitiveness gains also lagged programme projections amid increasing difficulties in political stability and administrative capacity that the Greek government faced in implementing structural reforms (European Commission 2012: 1). Against this deteriorating economic outlook, negotiations for a second adjustment programme were initiated.

Negotiations were not easy and often stormy. Talks between international creditors and the Greek government were repeatedly contentious over budgetary measures, including those related to the reduction of minimum wages and the elimination of salary bonuses granted to private sector workers (see, e.g. *Financial Times* 2012a). The question of how to reduce Greece's debt also stood front and centre, especially in the autumn of 2011, when fears of contagion gripped the eurozone. On 27 October, the eurogroup announced a series of measures to restore financial stability, including a 'voluntary' agreement with Greek private creditors to reduce the value of outstanding debt[18] – a measure that would be inserted in the second adjustment programme.

Germany was a tough negotiator from the beginning. In the months that preceded the first adjustment programme, the German government played a key role in ensuring that the Greek bailout would not be mistaken for unconditional support from eurozone partners. To achieve this goal, 'the only strategy that would work [from Merkel's perspective] was to demand that Greece impose severe domestic policies as a condition for the bailout' (Bastasin 2014: 193). The same emphasis on domestic discipline was articulated in the second round of negotiations. For instance, in one of the proposals circulated during the negotiations for the new memorandum of understanding in early 2012, Germany suggested the creation of a euro area 'budget commissioner' with the power to veto budget decisions taken by the Greek government if they were not in line with targets set by international lenders (*Financial Times* 2012a). Germany's position was far from being an isolated voice, and eurozone countries displayed a highly cohesive front towards Greece. This was particularly evident in November 2011 when the Greek prime minister, George Papandreou, floated the idea of putting the proposed bailout programme to a popular vote. On that occasion, he 'was stunned by the outpouring of anger from EU leaders' at a meeting convened in Cannes to discuss the matter (Spiegel 2014). At that juncture, France and Germany were closely aligned and the strategy on how to address Greek political leadership was carefully coordinated (Bastasin 2012: 336).

Despite this tough stance towards Greece, eurozone finance ministers eventually and quickly agreed upon a second rescue package at the end of February. Specifically, eurozone countries committed to disburse up to €130 billion through the EFSF, until 2014.[19] The IMF also contributed to the financing package with additional funding. As part of the agreement, the private sector accepted losses on its holdings of Greek debt. Furthermore, and in line with the previous programme, structural reforms were required in labour, product and service markets.[20]

That there was agreement on the second programme should not be taken for granted, especially when analysed from the German perspective. Indeed, the German government, and in particular Chancellor Merkel, pushed the agreement on a reluctant political base. Christian Democratic Union/Christian Socialist Union (CDU/CSU) members of the Bundestag were particularly concerned about the prospect of more financing along the way, especially in light of shaky pledges of fiscal discipline from the Greek authorities. The conservative *Frankfurter Allgemeine Zeitung* well summarized these concerns in the final stages of the negotiations, noting, 'Additional aid for Athens is unavoidable … Greece and other nations in crisis continue to live beyond their means, spending significantly more than they earn even though they actually need a surplus' (as translated in Spiegel Online International 2012a). The risk of continuing to throw good money after bad is evident in the positioning of several members of the CDU/CSU parliamentary group. For instance, Thomas Silberhorn of the CSU was reported as saying, 'if we don't limit the financial assistance, we will run up against the limits of political acceptance'. Striking a similar note, Transport Minister Peter Ramsauer (CSU) announced he would only agree to the Greek aid package 'with fists clenched in my pockets' (Spiegel Online International 2012b). The outcome of the vote on the second bailout showcased how fragile the political support for the German government was. 'Within the CDU/CSU bloc, 13 politicians rejected the bailout, with four members of the FDP [Free Democratic Party] joining them in opposition. Ultimately, Merkel had to rely on support from the opposition centre-left Social Democratic Party (SPD) and Greens' (Spiegel Online International 2012c). Even within the government, support for further financial assistance had been a divisive issue during the negotiations. This is well exemplified in the public stance of Finance Minister Wolfgang Schäuble, who had called into question Greece's commitment to austerity measures, and in the remarks of Peter Altmaier, one of Merkel's most important advisers, who also emphasized that Greek fiscal commitment was an 'extremely decisive prerequisite' for the release of further assistance (Spiegel Online International 2012d).

Despite the visible discontent in her political party, Merkel put her weight behind the second bailout by openly inviting the parliament to support the new programme (Spiegel Online International 2012e). This happened even though the second programme slowed the pace of fiscal adjustment in anticipation of the potential deflationary effects of the required structural reforms, especially those in the labour market (see Moschella 2016). In particular, the programme allowed a primary deficit of 1 per cent of GDP in 2012 and backloaded the bulk of fiscal adjustment to 2013–14.

Reading Merkel's stance against what would have happened in the third round of negotiations, it is thus plausible to argue that the chancellor had more room for manoeuvre to make concessions at the EU negotiating table in 2012 than would be the case just a few years later. Using the language of the two-level game, the preferences of the chief negotiator prevailed over the institutional constraints.

That Merkel's domestic constraints were not as binding as they were to become in the 2015 negotiations is also evident in the German position on the possibility of Greece exiting the monetary union – 'Grexit'. During the negotiations for the second adjustment programme, Schäuble had hinted at the possibility of Greece leaving the euro with enough financial support to stay in the EU (*Financial Times* 2015a). Interior Minister Hans-Peter Friedrich, a member of the CSU, was more direct, arguing openly for a Greek exit from the euro zone. As he told *Der Spiegel* at the end of February 2012, 'Greece's chances of regenerating itself and becoming competitive are surely greater outside the monetary union than if it remains in the euro area' (Spiegel Online International 2012b). In spite of the evident divisions in the government, the German chancellor rejected the Grexit option in 2012. 'We want Greece to stay in the euro', Merkel clearly spelled out after a meeting with French president, Nicholas Sarkozy (*Financial Times* 2012b), a position later reiterated in front of the parliament when agreement on the new bailout had been reached (Spiegel Online International (2012e).

The second adjustment programme quickly went off track. By October, a new standoff between international lenders and Greek authorities had developed over how to keep the bailout programme on track (*Financial Times* 2012c). In November, the eurogroup attempted to address the problem of Greek debt sustainability through a set of measures designed to ease Greece's debt burden. These measures included a reduction in the interest rate charged to Greece on the bilateral loans provided under the first adjustment programme, extending the maturity of the loans extended thus far by 15 years and deferring interest rate payments by 10 years (ESM 2015a). The programme survived its rocky start, but new problems lay ahead.

The situation deteriorated at the end of 2014 when the Greek prime minister, Antonis Samaras, brought the presidential election forward by two months after eurozone finance ministers concluded that Greece had not completed all the reforms necessary to obtain its last bailout payment and complete the programme. Specifically, on 19 December, the EFSF Board extended the programme until the end of February 2015 (EFSF 2014).

In the meantime, January elections brought Alexis Tsipras to power, the Syriza party leader who vowed to end fiscal austerity and renegotiate Greece's government debt if his party came to power. In line with his electoral pledges, once in power, Tsipras refused to seek an extension of the second adjustment programme and asked instead for a new agreement that would contemplate significant debt relief. Eventually, eurozone partners decided on a further extension until 30 June 2015.

At the end of June, however, negotiations on the second adjustment programme eventually collapsed following the Greek decision to call a surprise referendum on the programme's conditions. In the July vote, Greeks overwhelmingly rejected the bailout. However, Tsipras was also mandated to negotiate a new programme. It was the beginning of a third and tougher round of negotiations.

The Toughening: The Third Adjustment Programme

Negotiations for a third adjustment programme took place in a different institutional context from the one within which previous adjustment programmes had been agreed: the ESM had come into force in September 2012. Furthermore, the IMF signalled that it could no longer join the creditors' camp, as Greece no longer qualified for support because of its high debt levels and its poor record of reforms.[21] This is the institutional context within which Greek authorities negotiated what has been dubbed 'the most intrusive economic supervision programme ever mounted in the EU' (*Financial Times* 2015b; see also *The Economist* 2015). The proposal required Greek authorities to pass new reform laws on taxes and pensions and to introduce labour market liberalization. The government was also asked to reverse some of the spending measures it had introduced since the elections and to set up a trust that would be used to pay for bank recapitalization and to repay debt (*Financial Times* 2015c).

The hardening of the creditors' requests reflects the need to concede to national parliaments and, in particular, the Bundestag. As the *Financial Times* aptly observed, 'German MPs' views [now became] critically important because parliament must approve any deal that involves lending Athens more money' (*Financial Times* 2015d). The Bundestag, in turn, was in no mood to provide Greece with further assistance. Rather, as had been the case for the 2012 negotiations, German parliamentarians had deep reservations about the bailout. This is especially evident in the public posturing of CDU/CSU members – although SPD members shared most of the reservations as detailed below. In particular, members of Chancellor Merkel's CDU voiced doubts about the new Greek government's commitment to reforms and about the strategy of keeping financing the country (Handelsblatt Global Edition 2015a).

While no government in a parliamentary democracy can easily gloss over the concerns of the parties that support it, in the case under investigation the voice from the Bundestag became even more difficult to ignore as its members were now called on to approve the beginning of the third round of negotiations. The increasing attention to the preferences of national lawmakers was clearly detectable in the evolution of Merkel's negotiating stance. As the negotiations with the Greek authorities proceeded, the German chancellor explicitly stated that for her to 'recommend with full conviction' any deal to the German parliament, the Greek authorities should have taken steps to implement the suggested reforms (*Financial Times* 2015b) – implying that she could not compromise on further concessions as the bailout terms had to accommodate most of the sceptics in her conservative bloc (*Financial Times* 2015e).[22]

At the same time, and as a sign of increased brinkmanship compared to previous negotiations, Merkel moved closer to the negotiating position of her hawkish finance minister. For instance, when Schäuble proposed a possible five-year timeout from the eurozone for Greece (*Financial Times* 2015f), Merkel did not overrule the suggestion as she had back in 2012, but instead backed it in front of the Bundestag, where she presented a 'voluntary, organized Grexit as a viable option' (*Financial*

Times 2015g).

While Merkel's tougher stance could be ascribed to negotiation fatigue and to her change of mind on the need to keep Greece in the eurozone, several accounts indicate that this was political posturing rather than to a change in political preferences. Indeed, it is difficult to conclude that Merkel now became convinced that pushing Greece out of the eurozone was the best way of dealing with the crisis. In the middle of the July negotiations, she was still concerned at the prospect of European disintegration, not least for its impact on her historical legacy (Spiegel Online International 2015f). Furthermore, Merkel continued justifying the negotiations in light of the decision taken by eurozone leaders to rule out 'Grexit' (Handelsblatt Global Edition 2015b). In other words, as had been the case in 2012, Merkel's preferences were inclined towards a compromise.

In contrast to 2012, however, discontent in her party and government was more constraining at the EU table because of the Bundestag's formal involvement in the procedure through which financial assistance would be disbursed. Furthermore, opposition to financial support for Greece was not confined to CDU/CSU Bundestag members. Greece's decision to abandon the negotiations and call a referendum had alienated several Social Democrats too (Handelsblatt Global Edition 2015c). In a sign of growing discomfort in the Social Democratic Party (SPD) camp, Sigmar Gabriel, the party leader, told the *Tagesspiegel* newspaper that Greek premier Tsipras had 'pulled down the last bridges over which Europe and Greece could have moved to a compromise' (quoted in *Financial Times* 2015h).

In this changed institutional context, the hawkish stance of some members of her government became more influential on Merkel's negotiating stance than in the previous negotiation round. For instance, asked about Schäuble's comment that he was prepared to resign if he was ever forced to take a position on Greece that he did not agree with, Merkel replied that 'the finance minister will now lead these negotiations just as I will', adding, 'We will now work together in this coalition and of course together in the [Christian Democratic] Union' (Handelsblatt Global Edition 2015b). The nod to Grexit should also be read as a further attempt by the chancellor to smooth over the differences within her party over Greece. Commenting on the parliamentary debate, Eckhardt Rehberg, the CDU's budget spokesman, said: 'The debate over a temporary Grexit has been important' (*Financial Times* 2015i), hinting at the chancellor's attempts to win the support of a growing pro-Grexit lobby in her CDU/CSU party.

The hardening of the German position, in turn, contributed to the fuelling of discontent in the creditors' camp. In particular, France became increasingly vocal in its discontent at the German approach to Greece and put its political weight alongside that of the European Commission in an attempt to keep Greece in the eurozone (e.g., *Financial Times* 2015f, 2015j).

The growing divisions in the creditors' camp are particularly evident in the debate that followed Germany's proposal to push Greece towards a temporary exit from the eurozone. Although Schäuble's tough stance was supported by several other small countries – stretching from the Netherlands to Finland to Estonia, and countries that had endured their own adjustment programmes (such as Spain, Portugal and Ireland) (*Financial Times* 2015k) – around the negotiating table, divisions became evident and vocal. In addition to France, Austria's Chancellor Werner Faymann criticized the tone of the debate, noting that 'Such humiliation [for Greece] cannot be' (*Financial Times* 2015e). The Italian finance minister expressed similar concerns (*La Stampa* 2015).

Several factors certainly contributed to shaping these political coalitions among eurozone governments, including the support of public opinion, political business cycles and economic conditions. This is particularly notable in Finland, one of German's closest ally on the negotiations, where the populist Finns Party threatened to resign from the coalition government if a Greek bailout went ahead (Financial Times 2015l). However, it is interesting to note that the emerging coalition for a more lenient approach to Greece included countries whose legislatures had not approved the outcome of the intergovernmental negotiation. Indeed, the French parliament voted at the start of the negotiations, although the vote was neither required nor legally binding (see Fromage 2015). The

Austrian parliament is required to vote only ex ante in the ESM procedure, while the Italian parliament is not involved at all (see Kreilinger 2015). In contrast, in the hard-line coalition were all the countries where the legislature is required to vote on the outcome of the negotiations – the Netherlands, Estonia and Spain (see Kreilinger 2015).

As the negotiations with the Greek authorities moved closer to a deal,[23] the German government's position did not relax. This hardened position stood in stark contrast to the more accommodative stance taken by other hawkish eurozone countries, most notably Finland, which was ready to accept a deal in early August (*Financial Times* 2015m). In contrast, however, Germany had yet to put the outcome of the negotiations to the vote of the Bundestag. In other words, the German government's room for concessions was much more constrained. As a result, the stance towards Greece could not have been significantly relaxed, even if it brought growing isolation at the negotiating table.

In this light, we can see the further last-minute pressure exerted by Angel Merkel on the Greek authorities. Indeed, the German chancellor reached out directly to the Greek prime minister to tell him that Germany was ready to provide Greece with a bridging loan but that more time was needed for bailout talks (*Financial Times* 2015n). When the deal with Greece had almost been finalized, Germany even put at risk the fragile agreement by openly criticizing the new deal as insufficient (*Financial Times* 2015o), while at the same time trying to persuade the IMF to participate in the programme[24] – participation that was regarded by many as necessary to sell the outcome of the negotiations to the Bundestag.

The chancellor was aware of the effects of Germany's harder stance in terms of growing isolation among euro area countries. However, as has been noted, 'the chancellor cannot be seen to be too accommodating for fear of making it harder to sell a deal to her increasingly sceptical conservative CDU/CSU bloc' (*Financial Times* 2015q).[25] In short, the Bundestag's involvement in the negotiations weighed heavily on the position taken by the German government, significantly constraining its ability to compromise and jeopardizing consensus-building among euro area countries.

CONCLUSIONS

In the George Orwell's *Animal Farm*, the moment when some animals become more equal than others marks the beginning of the end of the ideals that had supported the political project embodied by the animals' takeover of the farm. A similar moment can be discerned in the integration of EU crisis management. The involvement of some national parliaments in decisions pertaining to financial assistance has contributed to undermining the objectives that had motivated the creation of the crisis management system in the first place. Rather than helping restore EU solidarity and fill in a damaging institutional vacuum, the ESM provided a venue that nurtured political cleavages. In short, the democratic dysfunction associated with having some national parliaments more powerful than others has seriously challenged the utility of financial assistance and thus the integration process itself.

The negotiations of the Greek adjustment programme have provided the natural scenario for assessing the distorting dynamic associated with ESM decision-making. In particular, the negotiations for the third adjustment programme turned towards a hardened and divisive approach that had no counterpart in previous negotiating rounds. This is especially evident in the comparison of the German government's position over time, which hardened in conjunction with the empowerment of the Bundestag under the new EU crisis management framework. The incentive for division is also evident in the comparison of creditor countries at different stages of the negotiations, reflecting the various domestic constraints that each faced. The relaxation of the Finnish position towards Greece in the summer of 2015, despite the continuation of the German confrontational approach, is indicative in this regard: unlike the Bundestag, the Finnish parliament was not involved in the approval of the outcome of the intergovernmental negotiation.

In emphasizing the role played by the new institutional context in which the Greek negotiations took place, this article has not claimed that other factors were irrelevant to the negotiation process, not least the incoherent strategy of the Greek government (Tsebelis 2016), the interactions among the Troika institutions (Moschella 2016) or the ideas that informed the positioning of the German leadership (Bulmer 2014; Matthijs 2016). However, while each of these factors were important at different stages of the negotiations, they were in turn affected by the context in which they were operating. For instance, as the article illustrated, the negotiating approach of the German chancellor was strongly influenced by the progressive empowerment of the Bundestag under the ESM. Merkel moved closer to her finance minister's hawkish stance at exactly the time that the legislature's approval was required for financial assistance.

In order to isolate the influence of the domestic institutional constraints on the dynamics of the bailout negotiations, the article relied extensively on cross-time and selected cross-country comparisons. However, some limitations need to be acknowledged. In particular, the research design could not control for the peculiarities of the Germany–Greece relationship. Variations in the political relationship with programme countries might plausibly explain differences in negotiation patterns. Unfortunately, however, the scope for comparison is limited as the other recipients of financial assistance – Ireland and Portugal – were funded under the temporary EFSF (and before the involvement of national parliaments) and the ESM programme for Spain was directed at supporting the recapitalization of the country's banking sector only. A viable comparison with the case examined in this study could be the negotiations for the ESM programme for Cyprus in 2013. By controlling for the institutional factors, future research could thus ascertain the extent to which political relationships between countries affect European negotiations.

The findings of the article speak to a number of studies that examine the foundations of the EU integration process. To start with, the study speaks to the research agenda on new intergovernmentalism by showing that governments did not always possess almost monopolistic bargaining powers on key decisions for rescuing the EU integration project during the crisis. Some of these key decisions – such as the one pertaining to membership of the eurozone – were taken in a larger political arena where the national parliaments' involvement challenged the usual practices of deliberation and consensus-decision by governments acting at the EU level (Bickerton, Hodson and Puetter 2015). The article also provided empirical evidence for legal concerns that asymmetric powers provided to legislatures by virtue of national constitutional rules, case law and legislation can threaten the functioning of the monetary union (Fasone 2014). While this asymmetry is important, it has received limited attention thus far compared to other processes of differentiation in the EU (Schimmelfennig and Winzen 2014; Winzen and Schimmelfennig 2016). Future research is thus needed to ascertain why some countries decide to empower their national parliaments in EU-level negotiations, while others do not. Likewise, it will be important to ascertain whether national divergences exist as to the legislatures that overtly advocate for the expansion of their powers in European negotiations.

The findings of the article also contribute to the academic and political debate on the ways in which to fix democratic deficits in the EU political system. Specifically, the study strikes a note of caution on the well-established argument that the empowerment of national parliaments in EU policy-making is one of the most powerful antidotes to its legitimacy deficit and thus a safeguard for the integration project (Bellamy and Weale 2015) The findings here suggest that the positive effect of national parliaments' involvement in EU policy-making cannot be considered automatic: solidarity (and possibly integration) can also be negatively affected by such an involvement (see also Jones and Matthjis 2017). This is especially the case when such an involvement is uneven – as in the case analysed here. However, it is plausible to speculate that even a more egalitarian involvement of national parliaments could be just as problematic; at a time in which anti-Europeanist and populist forces are increasingly on the rise, having national parliaments decide on the level of intra-EU solidarity (especially under conditions of financial stress) is not a reassuring institutional fix to address the challenges that the EU integration project faces. The popular trope 'be careful what you wish for' could not been more accurate.

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NOTES

[1] Initially provided to countries with balance of payment problems in Central and Eastern Europe, financial assistance has ultimately been provided to euro area countries as well.

[2] In addition, the crisis showcased the lack of an institutional framework for managing banks' solvency crises. However, this article solely focuses on the institutional framework that deals with sovereigns' liquidity and solvency problems.

[3] As will be discussed at greater length below, under the new crisis management system, not all national parliaments are involved to the same extent in financial assistance decisions. Instead, the differentiated power that they are assigned stems from uneven national constitutional rules and legislation. See Fasone 2014; Kreilinger 2015.

[4] The Troika is the institutional arrangement through which the European Commission, the ECB and the IMF jointly administered financial adjustment programs.

[5] The analysis relies on the articles published by the *Financial Times* covering the negotiations in 2010, 2012 and 2015. Articles were retrieved through the *Financial Times* website and selected from those carrying the tag 'Greece debt crisis'. In addition to the *Financial Times* articles, and in order to focus in on the evolution of the German government's position in the negotiations, I used Factiva to retrieve the articles published on the websites Der Spiegel Online International (www.spiegel.de/international) and Handelsblatt Global, Germany's leading business daily (www.global.handelsblatt.com). In this case, I screened articles based on the combination of the words 'Bundestag' with 'Greece' or 'Greek crisis'. The interviews were conducted on the condition of anonymity. Hence, I do not use them to support the arguments but as background information only.

[6] As reported in Fabbrini (2015: 50 fn 3).

[7] Among many others, see Hug and König (2002) and Milner and Rosendorff (1996). For a recent attempt to establish whether binding domestic constraints increase governments' international bargaining power, see Rickard and Caraway (2014).

[8] For a measurement of domestic constraints see Konig and Slapin (2004).

[9] As of 2009, approximately 80 per cent of the central banks had full responsibility for decisions concerning the LoLR function (BIS 2009).

[10] While the theory is quite straightforward, moral hazard concerns and the distributive implications of financial assistance have always been thorny issues for the LoLR. For an overview of these issues, see Tucker (2014).

[11] Of course, although the debate on the LoLR at the international level gained momentum in the 1990s, it has more ancient roots. For instance, Kindleberger (1973).

[12] The EFSF was set up as a three-year private company under Luxembourg law.

[13] The ESM has been endowed with an effective lending capacity of €500 billion deriving from a capital stock of €700 billion, of which €80 billion is paid-in capital with the remaining €620 billion as callable capital. Funding is also obtained by issuing bonds or other debt instruments on the financial markets.

[14] It is important to note that the ESM Treaty contemplates an emergency procedure that requires a qualified majority of 85 per cent of the votes cast; the weighted vote of each ESM member state corresponds to its capital share in the ESM. This majority gives Germany, France and Italy the right to veto as the three largest economies of the euro area. The emergency procedure was not used in the Greek adjustment programme analysed here.

[15] Data on national parliaments' involvement are drawn from Kreilinger (2015). For an overview of the other constitutional decisions that have strengthened national parliaments in the ESM, see Fasone (2014: 19-22)

[16] The ESM was also used to recapitalize the Spanish banking sector in 2012 and to cover Cyprus's financing needs in 2013.

[17] Information on the content of the adjustment programmes for Greece is drawn from the IMF regular staff reports on Greece from 2010 to 2015. The reports are freely available on the IMF website.

[18] Euro Summit statement, Brussels, 26 October 2011.

[19] Statement by the eurogroup, 21 February 2012.

[20] For the technical details of the 2012 programme, see European Commission (2012).

[21] Greece also became the first advanced economy to miss a payment to the IMF in the 71-year history of the organization.

[22] It is worth recalling that when the Bundestag debated whether to start negotiations with Greece on a new bailout, 60 CDU/CSU MPs voted against and another five abstained.

[23] By early August, a basic agreement was reached around a programme whose main elements included spending cuts, administrative reform and privatization. Remaining unresolved issues included details of a privatization plan and proposals on how to raise the budget surplus.

[24] As reported in the *Financial Times* (2015p), ‘According to the summary [of IMF Executive Board meeting], Germany’s representative to the IMF board said Berlin ‘would have preferred the fund ... move in parallel’ with the eurozone bailout talks.’

[25] Financial Times, *Greece strikes outline of debt deal with creditors*, 11 August 2015

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