



Heavyweights Go Toe-to-Toe in Cyprus

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The financial crisis in Cyprus is, among other things, a stress test in relations between Europe and Russia. Thus far, neither has performed very well.

Relations between Washington and Moscow are currently in a sterile phase, and are likely to remain so for the foreseeable future. Europeans, on the other hand, like to claim they are much more effective in understanding and managing the Russians. But are they?

First off, contrary to popular perception, Russian dirty money did not corrupt Cyprus. Nicosia was a thriving international financial brothel long before the Russians arrived. Indeed, Russian oligarchs knew where to launder their loot because the KGB had used Nicosia for its transactions during the Cold War.

The financial mess on Cyprus is thus not the product of Russian money, but of parallel failures of European governance and of Greek Cypriot risk-taking. However, Russian (and Russophone) money certainly bulked up the problem, just as foreign funds did in Iceland, Ireland and on Wall Street. The Russians, in other words, added a bunch of zeros to the scale of the crisis, but they did not create it.

Now, Russian oligarchs and companies—many of them effectively national entities, like Gazprom—are facing significant losses on their Cypriot accounts. They are annoyed, as they had figured a Eurozone economy was ultimately insured by the German taxpayer.

They figured wrong. The Troika (a.k.a. the European Commission, European Central Bank, and the International Monetary Fund) negotiated a no-nonsense rescue package with the newly-elected government of the Republic of Cyprus. The Greek Cypriot administration initially tried to tax its population, rather than impose the entirety of the costs on foreigners (and risk them taking their dirty business elsewhere). The parliament in Nicosia, however, gagged on this idea, and the revised "bail-in" now pending will end up hitting the Russians hard.

Moscow has condemned not only the substance of the Troika package, but also the fact that EU institutions had negotiated the deal with an EU member state without Russian participation. It then demanded a three-way mechanism, of the Troika, Russia and Cyprus. Moscow, in other words, wanted a seat at the table of the European club, of which it is not member, and a seat equal to the entire club.

The problem on the other side was almost as bad. European elites—especially the Germans—have portrayed the Cyprus crisis as a morality play, with Russia the villain, rather than acknowledging a problem of their own making. Greek Cyprus was admitted to the European Union in 2004 both as a divided island and with the Greek side flagrantly outside of EU financial standards. Four years later it entered the Eurozone still unreformed. Imagine the Cayman Islands as the 51st state, without application of the U.S. Code to its banking sector.

Then, the EU seriously proposed to Moscow a takeover of Laiki Bank by Russian financial institutions. (Laiki is the second-largest bank on Cyprus and notorious for, among other things, laundering plane loads of cash for Slobodan Milosevic and his family.) The Russians were incredulous. They correctly saw the proposal as a European ploy to shift the liabilities of Laiki onto Russian shoulders. In Brussels, on the other hand, this was seen as Russia simply taking responsibility for Russian deposits.

Moscow therefore claimed the EU proposal treated Russia in a disrespectful and "neo-colonial" fashion, just what Moscow tends to say about Washington. Russian and German political commentaries on this dispute are entirely self-referential, with each side viewing the other in stereotypical and even clichéd terms.

As the crisis sorts itself out in the weeks to come, part of the broken crockery is likely to be the political "understanding" that exists between Europe and Russia. These days, the conversations between Moscow and European capitals are beginning to sound every bit as acrimonious as the ones taking place between Russia and the U.S.