Kevin Featherstone and Dimitris Papadimitriou

Manipulating Rules, Contesting Solutions: Europeanization and the Politics of Restructuring Olympic Airways

UNDER WHAT CONDITIONS DO SYSTEMS OF COMPLIANCE WITH international law lead to outcomes that are sub-optimal for each of the parties directly involved? The governance of the European Union (EU) is unique in its system of supranational law. As the EU’s executive agency, the European Commission is charged with regulating the internal market: an area in which it has been able to extend its authority incrementally, supported by the European Court of Justice (ECJ). The Commission’s role in the Union’s ‘competition policy’ has a complex, asymmetrical structure, however. Whilst in certain areas, such as the regulation of state aid, its institutional authority is supported by very strong compliance mechanisms, and in others it is backed by EU legislation to enforce market de-regulation; in matters of the overall policy agenda its capability rests on cooperation with the member states. It can thus insist or pull its punches on state subsidies, but it can only seek to build a consensus on specific supply-side solutions, such as privatization. The Commission’s role combines

1 The present article is part of an ongoing research project on Europeanization and structural reform in Greece. The authors would like to express their gratitude to the large number of actors within the sector in Athens – from government, unions and management – who made themselves available for personal interviews. The authors have respected their desire to remain anonymous. Moreover, invaluable comments have been received from seminar presentations given at the universities of Athens and Sheffield and at the ECPR Joint Sessions, 2005. Any errors remain ours.

specific areas of authority alongside a wider set of preferences and strategy based on softer mechanisms.

Within their own domain, member governments are liable to constraints (inter alia) of the electoral cycle, state patronage and clientelism, and the power of organized interests. Governments may share with the Commission goals such as the restructuring of state enterprises, but themselves be limited in their abilities to deliver such outcomes. Heavy state indebtedness can establish the logic of restructuring a major loss-making enterprise (and proceeding to its privatization), but domestic political conditions can oblige a government to seek to manipulate EU rules on state aids in order to ease the otherwise painful transition. A game akin to ‘cat and mouse’ may ensue with the Commission. The latter cannot properly engage in an evaluation of all feasible domestic reform options or the ‘win-sets’ of national actors; rather, it must assess the use of state aids in a particular case against a general backdrop of prohibition. It has a strong negative power – able to veto solutions – but a weak proactive capability in restructuring policy debates. Moreover, the process of Commission investigation and possible subsequent challenge by member states in the ECJ can be a lengthy – and, by its nature, an uncertain – one.

This is a case study of where two key actors – the EU Commission and the Greek government – proclaimed compatible policy goals, but where their respective institutional constraints prevented them from cooperating to achieve them. The case is the attempt of the PASOK (socialist) government (under Prime Minister Costas Simitis, 1996–2004) to restructure the ailing national flag-carrier, Olympic Airways, in parallel to the EU’s agenda of market liberalization of the air transport sector in the 1990s. Whilst the Greek government pursued a variety of reforms after 1994, the paper focuses primarily on the events culminating in the 2003 initiative (the ‘Verelis Law’) to create the new ‘Olympic Airlines’. This led to a breakdown in the previous policy of tentative cooperation between Brussels and Athens, with an investigation by the Commission and a legal challenge in the ECJ – a process that took more than three years and eventually resulted in a legal victory for the Commission. This article traces the failure of cooperation and seeks to explain the result of a sub-optimal bargaining outcome. The empirical analysis is placed within the conceptual framework of Europeanization and models of compliance.
Europeanization and Non-Compliance

There are two critical dimensions to this case study: firstly, the strategic interaction between the European Commission and the Greek government; and secondly, the interaction between the Greek government and domestic actors with veto-potential.3 The Simitis government stood astride both, its strategy determined by the ‘nesting’ of the two arenas.4 The literature on Europeanization and domestic non-compliance has focused on similar cases. Moreover, across EU policy sectors, Greece has been a disproportionately high offender5 and it exhibits many of the features associated with implementation failure.6 Greece is thus a critical case by which to examine how the impact of the Commission’s actions is affected by domestic impediments to reform.

Studies of domestic non-compliance have given rise to a number of explanatory hypotheses, developed in the main in the environmental policy sector. A group of authors have applied the notion of ‘fit’ or ‘misfit’ between EU rules, on the one hand, and the domestic institutional and regulatory setting.7 In this vein, Börzel developed a ‘push-pull model’, where non-compliance is ‘most likely if an EU policy causes a significant “policy misfit” and if there is no mobilization of domestic

3 The individual or collective actors who must agree to the change before it can happen, see G. Tsebelis, Veto Players: How Political Institutions Work, Princeton, NJ, Princeton University Press, 2002, p. 19.

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actors pressurizing public authorities to bear the costs of implementing the “misfitting” policy. Haverland went further in his coverage of the domestic institutional opportunity structure: unwilling governments can be pushed to comply or governments may be willing but blocked by domestic actors able to veto. Heritier et al. expanded the focus to a catalogue of factors, including the ‘reform capacity’ of a member state. The latter is determined by supportive actor coalitions and veto players. The relevance of veto players to policy outcomes has been most prominently developed, in comparative politics, by Tsebelis. He has argued that ‘policy stability’ (the impossibility for significant departures from the status quo) is more likely the higher the number of veto players and the greater the (ideological) distance between them. In something of a synthetic work, Falkner et al. have developed a typology of ‘three worlds of compliance’. These are intended to overcome the inadequacy of single hypotheses. They posit ‘three worlds of compliance’: a world of law compliance (in which priority is attached to law compliance above domestic concerns); a world of domestic politics (in which obeying EU rules is one goal amongst many and domestic concerns frequently prevail); and a world of neglect (in which EU compliance is not a goal in itself). As the authors acknowledge, culture is a dominant factor in the world of law observance, whilst interests predominate in the other two worlds.

The case of Olympic Airways sheds light on the relevance of a number of these approaches. This is a case of initially proximate preferences on the part of the Commission and the national government: both accepted it as a ‘misfit’ and viewed the status quo as too costly. It is not, therefore, a case of the unwillingness of the government to pursue reform. Neither is it a case where domestic mobilization in support of reform was at a level greater than that of

8 Börzel, ‘Why There is no “Southern Problem”’, p. 141.
11 Tsebelis, Veto Players, pp. 2–3 and 11–12.
13 See Knill, ‘European Policies’.

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government.\textsuperscript{14} Against this background, the failure to pursue reform is best understood by reference to domestic blockages\textsuperscript{15} as well as by the inability of the Commission and the Greek government to adjust their strategies in order to achieve their seemingly shared objectives.

With regard to domestic impediments, Falkner et al. are right to point to the weak culture of law observance that leaves policy outcomes to be determined by the ‘domestic politics’ of veto players and their interaction.\textsuperscript{16} Indeed, they noted in their case study of the transposition of EU labour laws that ‘neglect’ was the common feature of all phases of the implementation process in Greece.\textsuperscript{17} In the case of Olympic Airways, the capacity of the government to implement change was further constrained by militant unionism, the company’s weak management structures and a myriad of sectoral interests accumulated by a long history of party political interventions in the Greek flag-carrier.

Against such a dense network of domestic veto players, the European Commission offered, in principle, a valuable ally for the Greek government in its expressed will to reform Olympic. The Commission is a central player in the enforcement of EU competition and state aid rules. The precise interpretation of these rules, however, is often hotly contested and their enforcement requires lengthy and delicate negotiations between the Commission and offending member state(s). Such an uncertainty becomes all the more pertinent in areas of the Single European Market – such as air transport – where liberalization is still ongoing. As the Commission’s own preferences on the content, speed and policing of this agenda are constantly reviewed, the signals national governments receive from Brussels vary over time. The turbulent relationship between the Greek government and the Commission over the reform of Olympic Airways cannot be fully understood without reference to this uncertainty.

Hence, this case study suggests the relevance of the following hypotheses. The EU’s commitments against state aids and on competition policy provide the Commission with an authority to impose compliance in pursuit of a liberalizing agenda. This agenda may be

\textsuperscript{14} See Börzel, ‘Why There is no “Southern Problem”’.  
\textsuperscript{15} Haverland, ‘National Adaptation to the European Union’.  
\textsuperscript{16} Falkner, Treib and Hartlapp, ‘Worlds of Compliance’.  
shared by a member state government when it is faced with a heavily indebted state enterprise, such as a national flag carrier. However, 

(1) When confronted with multiple veto players at home, national governments will choose to abort cooperation with the European Commission and opt for unilateral policy solutions that risk facing the consequences of non-compliance with EU rules. 

(2) Conflict between the Commission and national governments is more likely when the Commission itself emits inconsistent and/or confusing signals to the member government as to the range of solutions it will rule acceptable.

Both hypotheses raise questions about the ability of the Commission to steer an EU-wide agenda of economic reform and the ‘reform capacity’ of a member state such as Greece to deliver on EU-level commitments.

The European Commission as an Actor in the Domestic Reform Process

With its unique juxtaposition of roles and complex variety of competences, the Commission is both a referee and a player in the process of market liberalization. The Commission’s competence to act in the air transport sector derives from several sources: the treaty provisions on transport, its powers to intervene on market-distorting ‘state aids’, and the application of internal market liberalization measures to the sector. Air transport in the EU was liberalized in three successive stages: with a first package of measures adopted in 1987 and a second in 1990, and with the final and more substantive third package adopted in 1992 and applied as from January 1993. The ‘third package’ gradually introduced the freedom to provide services within the EU and led in April 1997 to the freedom to provide cabotage, that is, the right for an airline of one member state to operate a route within another member state. It comprised: common rules on the licensing of air carriers, rules on access for Community air carriers to intra-Community air routes, rules on fares and rates for intra-Community air services and the full application of the competition rules of the Treaty to the liberalized air transport market.18

18 For further background information, see: http://www.europa.eu.int/comm/transport/air/rules/competition_en.htm.
In the general area of competition policy, the Commission’s role is an exception from the wider norm: it has supranational authority to act and the objects of regulation are the national governments themselves.\textsuperscript{19} Within this regulatory framework, however, a key element is the Commission’s bargaining, on a bilateral basis, with national governments in relation to industry restructuring. The bargaining process requires the Commission to elaborate its priorities, strategies and tactics, providing scope for interpretation and adjustment. The latter is, inevitably, affected by changing political agendas and leadership personalities. By the 1990s, the stress was undoubtedly on de-regulation and the abandonment of state aids distorting competition. Loyola De Palacio, the transport commissioner from September 1999 to November 2004, pursued her strategy with vigour, at times heightening the sense of confrontation with member governments.\textsuperscript{20} In addition to Olympic, the Commission has been embroiled in disputes concerning the restructuring of Air France, Alitalia and Iberia airlines.\textsuperscript{21}

The Commission acknowledged implicitly the sensitivities that would arise if it were to call directly for privatization in the sector, but its repeated assertion of the need for a fully liberalized European market and its insistence that state intervention (in the form of aid, subsidies and patronage) should end showed a clear stimulus to national flag-carriers being run on fully commercial lines. The Commission went as far as it could to structure the reform path: indeed, in 1994 it had granted aid to various European companies, ‘which would allow . . . their possible privatisation’.\textsuperscript{22} Loyola De Palacio, as the relevant commissioner, was clearly frustrated by the lack of reform and the lack of transparency in accounting in the case of Olympic Airways.\textsuperscript{23}


\textsuperscript{20} Loyola De Palacio was a leading member of the centre-right Partido Popular in Spain, having previously served as minister of agriculture and as a member of the European Parliament (briefly). She was appointed as vice-president of the Commission, responsible for relations with the European Parliament, alongside the Transport and Energy portfolios, under President Romano Prodi. Previously, Neil Kinnock, formerly leader of the British Labour Party, held the Transport portfolio in the Commission of Jacques Santer, 1995–99.


\textsuperscript{22} European Parliament Questions, 16 November 1999.

\textsuperscript{23} Ibid.
The Commission’s approach was outlined by De Palacio at the World Economic Forum:

. . . Europe’s airline industry and economy was not strengthened by unquestioning national support for inefficient national flag carriers and the building of national champions – on the contrary, it was actually weakened. We have seen how difficult Olympic Airways and TAP have found it to develop a successful long-term strategy in spite of state aid and restructuring plans . . .

Ten years after liberalisation [the establishment of an internal market for transport services in 1992], the true benefits of a clear focus on a liberalised European market – and not on specific airlines – are becoming clear for European consumers . . . Our initial objective is to maintain and improve the liberalised European marketplace [emphases in original].

The preferences of the Commission can be inferred from such public statements: the will to act was clear. The Commission’s stress was on efficiency, competition, the abandonment of state aids – broadly defined – and a vibrant European marketplace.

This is a case, therefore, that begins with the Commission taking action over the use of state aids. Indeed, it remains the central basis of the Commission’s competence to act as the case develops. However, over time, the Commission also gave important signals of its preferences in relation to domestic privatization. No national government could have failed to recognize the existence of the latter or to have understood that they would serve to define, in part, the range of acceptable policy solutions when flexibility on state aid rules was being sought.

Yet, criticisms of the Commission’s performance in this area could also create some doubt as to its future intentions. Some suggest that liberalization in this sector has been ‘one of the Commission’s success stories’. However, whilst considerable progress has been made in removing the internal market barriers within the sector, a greater coherence in the system of regulation has been called for. More generally, well-publicized disputes over the Commission’s

decisions on company mergers, under EU competition policy, have provoked ‘increasing public criticism about the quality of analysis underpinning some . . . decisions’. 28 This has been sharpened by ECJ rulings overturning Commission vetoes on mergers. These factors would give member governments additional reason – over and above their domestic constraints – to review carefully the signals emanating from the Commission and to its decisions.

THE DOMESTIC SETTING: THE POLITICS OF NON-MANAGEMENT

Whilst the interests and strategies of the Greek government are to be understood with reference to the ‘nesting’ of the EU and the domestic arenas, at home the institutional setting of the Olympic case reflects a triangular structure covering government, management and unions. The complexities and asymmetries within this structure have largely determined the success of the action taken in relation to the company.

The capability of Greek governments to deliver substantive reform has long been in question, given the nature of state institutions, the power of vested interests and the political culture of clientelism and corruption. 29 In an earlier period, Lavdas and Ioakimidis 30 outlined the nature of Europeanization in Greece. There is a very limited literature on the politics of privatization in Greece, however. 31


31 Indeed, there is a very limited literature on privatization in general in Greece. Haritakis and Pitelis noted that the ‘particularly inefficient and corrupt public sector’ creates a need for privatisation in Greece (N. Haritakis and C. Pitelis, ‘Privatisation in Greece’, in D. Parker (ed.), Privatisation in the European Union: Theory and Policy
The transformation of Olympic Airways (OA) from a privately run airline to a public utility (Δημόσιος Οργανισμός Κοινής Οφέλειας, ΔΕΚΟ/DEKO) in 1975 opened a new chapter for the company’s history. Political parties, the state bureaucracy and a myriad of sectoral interests both in Greece and abroad have all, under the pretext of OA’s ‘national mission’, sought to use Olympic as a tool for political expediency and easy money-making. Despite the accumulation of heavy debts since the late 1970s, Olympic’s status as a public utility made the monitoring of its financial position almost impossible since its management was not required to produce detailed accounts. The picture of OA’s finances was further blurred by the fact that the Greek state chose not to pursue the company’s huge tax and national insurance arrears and Olympic was not required to pay airport taxes and handling charges.

The highly clientelistic practices and interventionist strategies of successive Greek governments produced highly unstable management structures for Olympic Airways. In the 30 years under government control, the top management (i.e. the chairman and/or the CEO) of Olympic Airways has changed 31 (sic) times, often filled with candidates that had little or no experience in the industry. The OA’s board of directors has also been a dysfunctional and unstable body.

Perspectives, London, Routledge, 1998, p. 134). Clifton et al. argued that the ‘overriding reason for [privatization] was to reach the convergence criterion to participate in EMU (J. Clifton, F. Comin and D. D. Fuentes, Privatisation in the European Union: Public Enterprises and Integration, London, Kluwer, 2003, p. 69). Indeed, Lavdas was surely correct to note that, ‘Economic liberalization and Europeanization have been the twin processes gradually reshaping the political economies of the European South since the 1980s’ (K. Lavdas, ‘The Political Economy of Privatization in Southern Europe’, in D. Braddock and D. Foster (eds), Privatization: Social Science Themes and Perspectives, Aldershot, Dartmouth, 1996, pp. 233–60, p. 254). More directly relevant is G. Pagoulatos’s study (‘The Enemy Within: Intragovernmental Politics and Organizational Failure in Greek Privatization’, Public Administration, 79: 1 (2001), pp. 125–46) of the privatization attempts of the earlier (centre-right) Mitsotakis government. He argued that policy failure was the result of such a concentration and the irony of a statist, impositional strategy for market liberalization. Pagoulatos’s case study highlighted particular features of administrative ill coordination (indeed ‘intragovernmental feudalisation’, p. 138), lack of policy preparation, the isolation of key technocratic advisers, and the cavalier and arrogant attitude of ministers – key factors undermining effectiveness and coherence. These factors were of little relevance in the present case study, however.

Olympic Airways (OA) was founded as a private enterprise in 1957 by the Greek magnate Aristotle Onassis. The company was sold to the Greek state on 26 June 1975.
Filled with party-political appointees, ministry bureaucrats and union representatives (in a non-executive capacity), the membership of the board changed very frequently and its members did little to justify the substantial fee they received in order to attend the board meetings. The net result of this cacophony was, more often than not, a managerial paralysis with no chairman or CEO of Olympic being able to work with a board that was not directly or indirectly controlled by the government.

The relation between Olympic’s management and their political masters has thus been one of convenience and subservience. Whilst the OA’s management was expected to run the day-to-day business of the company, ministers were heavily involved in all major decisions affecting the future of Olympic, often with blatant disregard for management’s authority and judgement. The government’s increasing reliance on external consultants to perform even the most routine management tasks within the OA group has been indicative of this. In the very few cases where the airline’s management sought to assert its authority against the government, the latter was always quick to restore order by sacking those with a more independent disposition.

The relationship between government and the unions of OA, on the other hand, reflected the weaknesses of the wider system of Greek labour relations. Within this system, interest mediation has typically been characterized by ‘rent-seeking’ behaviour – with sectional interests competing for favours, resources and subsidies\(^{33}\) – and a ‘disjointed corporatism’\(^{34}\). Specifically within the OA group, a total of 17 sectoral unions have operated, reflecting the very diverse range of activities (aviation, technical, handling and administrative) performed by its numerous subsidiaries. All 17 sectoral unions formed

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part of the Federation of Civil Aviation Unions (Ομοσπονδία Σωματείων Πολιτικής Αεροπορίας, ΟΣΠΟ/OSPA), the umbrella union for the entire workforce of the OA group. Traditionally, internal union politics were dominated by the divide between ground staff, on the one hand, and the pilots and cabin crew, on the other. Nevertheless, OA’s unions have been remarkably united in the fierce defence of their employment conditions (which are widely regarded to be more privileged than those enjoyed by Olympic’s international and domestic competitors) and militantly opposed to the prospect of the Greek flag-carrier slimming down its operations or losing its state-owned character.

In the post-Onassis period, the unions’ influence in the running of Olympic grew. Union leaders acquired direct access to ministers, often without the knowledge of the OA chairman/CEO’s knowledge. During the 1980s union strength became all the more evident, as the influential mistress and later wife of Prime Minister Andreas Papandreou, Dimitra, herself a leading figure in the flight attendants’ union (EISF), encouraged a more maximalist union agenda and rewarded her former colleagues with a number of extra privileges (through the so-called ‘Dimitra laws’). Then, in 1994, a new law gave OSPA two non-executive seats on the OA board, allowing its unions direct and formal access to company management decisions.

The net effect, in strategic terms, was of the contest between ministers and the unions, with the latter as de facto veto players pursuing a reactive and defensive strategy. Whilst this interaction was crucial to the outcome, the strategies of both government and the unions were affected by two wider contextual factors. The first is the pervasive influence of clientelism and the impact this had on strength of government purpose. When reform attempts increased the political ‘heat’ by threatening established political interests, some members of the government and of the wider (PASOK) party grew nervous and questioned the benefits of the strategy. The electoral interest was obvious: most of the OA current or former employees and their families lived and voted in the key second Athens constituency (Athens B) where 43 of the 300 members of the Greek parliament stood for election. Governments saw OA as a vehicle for extensive clientelism and regularly interfered with personnel matters. Privatization challenged established political interests and practice. The second factor is that, at best, public opinion seemed ambiguous on the question of privatizing Olympic. The airline was a source of
regular complaint amongst travellers. Yet, successful privatization here might threaten the security of employment for other public sector workers and it would challenge the myriad contracts and privileges connecting networks of suppliers and travel agents. The government’s rhetoric had elicited no significant reform coalition. Instead, there was a reservoir of public affection for the national flag-carrier and a strong sensitivity to its social role in maintaining loss-making routes between Athens and isolated islands.\textsuperscript{35} The consequence of internal government dissension and public ambivalence was that ministerial reformers were left isolated in their battle with the unions: their strategic calculations had to recognize the narrowness and shallowness of their support.

NO KNOWN CURE? THE ATTEMPTS TO REFORM OLYMPIC AIRWAYS, 1994–2000

The starting point for the present case study is the agreement in October 1994 between the PASOK government of Andreas Papandreou and the Commission concerning a rescue plan for OA. With its agreement, the Commission had sanctioned the second largest airline bailout\textsuperscript{36} – behind only that of Air France – and had engaged in a process akin to a shared management of the problem.\textsuperscript{37} As part of the agreement, the Greek government was obliged to introduce a new law (2271/94) involving substantial cuts in staffing costs, a rethink of OA’s international routes and the full implementation of the EU’s third air transport package by the end of 1994. Crucially, the Greek government also promised to put an end to its interference with the management of OA and grant the airline the full status of a private company. These commitments would come to haunt the government in Athens.

\textsuperscript{35} Doganis, \textit{The Airline Industry in the 21st Century.}

\textsuperscript{36} The proposals of the Greek government for Olympic provided for: (a) the write-off of ECU1.4 billion (GDR427 billion) of accumulated debt; (b) the conversion of ECU209 million (GDR64 billion) of debt into equity; (c) a capital injection of ECU177 million (GDR54 billion) in three yearly instalments between 1995 and 1997; and (d) the extension of ECU300 million (GDR91.6 billion) of state guarantees to Olympic until the end of 1997.

The implementation of the plan, however, soon ran into serious difficulties following fierce union opposition and constant changes in the management structures of Olympic. Against this background, the Commission refused to authorize the release of the second instalment of the government’s planned capital injection to Olympic worth ECU75 million (GDR23 billion) in April 1996. In its decision, the Commission drew a distinction between its view of the actions of the government and those of the company. Whilst the Commission stated that the airline had met the obligations imposed on it in the context of the 1994 agreement, the Greek government had defaulted, by continuing to interfere in the management of OA and providing unauthorized state aid of ECU36 million (GDR11 billion). The crisis of 1996 sent a strong message of the Commission’s increasing activism: Brussels’s gatekeepers would, from then on, shape the future of Olympic Airways in ways that the Greek government seemed unable (or unwilling) to comprehend.

As the financial position of Olympic continued to deteriorate in 1996 and 1997, the Greek government did little to honour its commitments to restructure the airline. The reform of Olympic only re-emerged in early 1998 within the context of Greece’s effort’s to convince its EU counterparts as to the merits of its membership of ERM II and its commitment to enforce fiscal discipline on its public utilities. In April 1998, amidst fierce union opposition, the government pushed through parliament a new law (2602/98) for the restructuring of Olympic Airways that introduced more flexible working practices and cost-cutting measures. Keen to encourage the Greek government’s tentative efforts for reform, the Commission agreed to release the second instalment (worth ECU41 million/GDR 14 billion) of the 1994 aid package. Brussels and Athens were, once again, signing for the same hymn sheet.

39 Eleftherotypia, 30 April 1996.
41 Greece entered ERM II on 14 March 1998.
In a separate development, the Greek government now attempted another solution for OA – by tying it to a strategic partner overseas. In June 1999, a deal with British Airways (BA) via its consultancy subsidiary, Speedwing, was announced. Speedwing would take over the management of OA until the end of 2001, for an estimated fee of £7 million and Rod Lynch, a former BA director, was appointed chief executive of OA. Crucially the deal also included a clause allowing British Airways to purchase a 20 per cent stake in Olympic once the operations of Olympic were streamlined by the new management. But, by the time the new management arrived, the situation in Olympic had once again become untenable. Many of the provisions of the 1998 restructuring plan had effectively been cancelled by subsequent agreements between OA’s former management and the unions, and the airline’s losses for 1999 were estimated as in excess of €75 million (GDR25.9 billion). OA’s finances received another blow in the summer months of 1999 following continuous strike action from the OA union opposing the deal with Speedwing.

The blueprint of the BA managers for the future of Olympic was published in October 1999; in effect, the third restructuring plan since 1994 (see Figure 1). Central to the vision of the new management was the expansion of Olympic’s operations (and a 1,000-strong increase of its workforce) as part of a major drive to win back passenger numbers. To finance this expansion, Speedwing planned a mixture of borrowing and asset selling. Speedwing’s ambitious plans afforded Rod Lynch a precarious truce with the powerful pilots’ (EXPA) and flight attendants’ (EISF) unions (but not OSPA) and the full support of the minister of transport, Tasos Mantelis. The Commission’s reaction, however, was much more sceptical since the new plan was regarded as a retreat from the agreements with the Greek government in 1994 and 1998. As a result, the third and final from the second and third instalments. During the same negotiations the Commission also authorized state loan guarantees of $378 million for the purchase of new aircraft for Olympic.

46 In 1999 OA employed 7,000 permanent and 3,000 seasonal staff. See To Vima, 14 April 2002.
### Figure 1

**Olympic Airways: a troubled history**

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
</tr>
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<tbody>
<tr>
<td>Jan. 1975</td>
<td>The Greek state takes over the ownership of Olympic Airways from Aristotle Onassis (Law 96/1976)</td>
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<td>Mar. 1994</td>
<td>The Commission announces investigation on illegal state aid to Olympic Airways</td>
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<tr>
<td>Oct. 1994</td>
<td>The Commission authorizes over ECU2 billion of state aid to Olympic Airways (in three instalments),</td>
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<td></td>
<td>conditional on restructuring the airline and the opening up of competition in the field of air transport</td>
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<tr>
<td>Nov. 1994</td>
<td>The Greek government passes Law 2271/94 on the restructuring of Olympic Airways</td>
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<td>May 1995</td>
<td>The first instalment of the aid package to OA is released</td>
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<td>Apr. 1996</td>
<td>The Commission refuses to authorize the release of the second instalment of aid to OA and launches</td>
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<td></td>
<td>investigation into illegal state aid by the Greek government since 1994</td>
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<tr>
<td>Apr. 1998</td>
<td>The Greek government passes Law 2602/98 on the restructuring of Olympic Airways</td>
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<tr>
<td>Jul. 1998</td>
<td>The Commission authorizes the release of the second instalment of the aid package to OA and drops the</td>
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<td></td>
<td>investigation into illegal state aid by the Greek government</td>
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<tr>
<td>Jun. 1999</td>
<td>The Greek government announces deal with British Airways for the management of Olympic Airways</td>
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<tr>
<td>Oct. 1999</td>
<td>The management of OA announces a new restructuring plan</td>
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<tr>
<td>Mar. 2000</td>
<td>The Commission refuses to authorize the release of the third instalment of aid to Olympic Airways</td>
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<tr>
<td>Jun. 2000</td>
<td>Deal between the Greek government and British Airways collapses</td>
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<td>Dec. 2000</td>
<td>The Greek government unveils tender for the sale of a majority stake of the entire Olympic Airways group</td>
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<tr>
<td>Feb. 2002</td>
<td>Privatization process collapses</td>
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<td></td>
<td>The flying operations of OA to be sold separately from the group’s subsidiaries</td>
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<td></td>
<td>government announces intention to appeal the decision to the ECJ</td>
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<tr>
<td>Feb. 2003</td>
<td>Privatization process collapses</td>
</tr>
<tr>
<td>Aug. 2003</td>
<td>The Greek government passes Law 3185/03 establishing Olympic Airlines</td>
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<tr>
<td>Jan. 2004</td>
<td>Olympic Airlines begins its operations</td>
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<tr>
<td>Mar. 2004</td>
<td>The Commission launches investigation on illegal state aid to Olympic Airways/Airlines by the Greek</td>
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<tr>
<td></td>
<td>government for the period since 2002</td>
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<tr>
<td>Jan. 2005</td>
<td>The Greek government unveils tender for the sale of a majority stake of Olympic Airlines</td>
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<tr>
<td>May 2005</td>
<td>The ECJ upholds the Commission’s decision on illegal state aid to Olympic for the period 1998–2002</td>
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<tr>
<td>Sep. 2005</td>
<td>The Commission rules that Olympic Airways had benefited from €540 million of illegal state aid by the</td>
</tr>
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<td></td>
<td>Greek government since 2002</td>
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instalment (worth ECU 22.8 million/GDR 7.8 billion) of the 1994 aid package was not released. For the British managers, the Commission’s obstructionism was a severe blow. With a general election scheduled less than six months away, Lynch had little time and money to prove that his ambitious gamble could turn the fortunes of Olympic around.

NOW YOU SEE IT, NOW YOU DON’T! THE BIRTH OF OLYMPIC AIRLINES

PASOK’s marginal election victory in 2000 brought to Simitis’s new cabinet a number of fresh faces, including the new minister of transport and telecommunications, Christos Verelis. A loyal supporter of the Greek premier, Verelis had built his reputation as an effective manager of public utilities and he was keen to prove his modernizing credentials to his new boss. Within weeks of his arrival in the ministry, Verelis announced the government’s intention to sell off a stake in Olympic Airways to the private sector and offered BA a 45-day deadline to exercise its option, under the 1999 deal, to buy a 20 per cent share in the airline. 48 The minister’s relationship with the British managers, however, was already showing signs of discord. Leaks to the press suggested that Verelis was critical of Speedwing and that he doubted the sincerity of BA in acquiring a stake in Olympic, particularly in the aftermath of Rod Eddington’s appointment as BA’s CEO in May 2000. 49 Thus, BA’s announcement, on 2 June 2000, that it was no longer pursuing the deal with Olympic came as no surprise. Less than a year after his arrival in Athens, Rod Lynch’s Olympic adventure was over as Speedwing’s managers were given two months to vacate their offices and leave the Greek airline. 50

The departure of the BA management marked a crucial turning point for Olympic and, as such, it has been open to conflicting interpretations. For Verelis, the termination of the BA deal was a natural conclusion of what he regarded as inept management and a lack of commitment on behalf of BA. To his opponents, however, Verelis had made a huge miscalculation. Many blamed him for being

48 Ta Nea, 19 May 2000.
49 Ta Nea, 3 May 2000.
50 Eleftherotypia, 5 June 2000.
too easily convinced by the unions’ complaints of Speedwing’s management and too ready to pass judgement on its performance. Even if the minister was dissatisfied with Lynch’s management, the 1999 agreement gave the Greek government the right to ask for his replacement (by BA), an option that was never used. Above all, Verelis stood accused of torpedoing the deal with BA without having secured a viable alternative. In the early 1990s, the Greek flag-carrier had repelled the possibility of an alliance with Lufthansa, now it had lost another suitor.

In response to the new situation, Verelis moved quickly to announce the sell-off of a majority stake (up to 65 per cent) of the whole Olympic Airways group (including subsidiaries) to a private investor who would also be solely responsible for the management of the airline. In an attempt to entice potential investors, Verelis also floated the idea that the government might be willing to assume all of Olympic’s debts. In the meantime, Verelis announced that an independent consultant (PriceWaterhouse Coopers) would undertake a financial audit of Olympic so as to offer transparency prior to the international tender for the sale of OA scheduled for late 2000. The new rescue plan for Olympic was received with dismay by the unions, which feared that the government was planning further job cuts and accused Verelis of trying to sell off the airline ‘on the cheap’.

As Verelis battled with OA’s unions at home, the reaction to his rescue plan in Brussels was mixed. The Commission had criticized the Greek government over its compensation to Olympic for the move to the new Athens airport (scheduled for 1 March 2000) and continued to withhold the third instalment of capital injection foreseen in 1994 restructuring plan. However, in the aftermath of Verelis’s meeting with commissioner for transport, Loyola De Palacio, in October 2000 the Greek minister appeared confident that the Commission would be willing to accept the write-off of OA’s debts – a perception that would prove critical later – provided that such a move would lead to transfer of the Greek flag-carrier to private hands. Encouraged by what he perceived as the Commission’s silent consent to his plan, Verelis pushed ahead with the publication of an international tender for the sale of the OA group in December 2000, with

51 Eleftherotypia, 7 July 2000; Ta Nea, 7 August 2000.
52 Eleftherotypia, 9 August 2000.
53 Eleftherotypia, 8 September 2000.
the promise that the Greek government would assume all past debts
of the airline and, crucially, would absorb any ‘excessive OA staff’ by
re-employing them in other services in the wider public sector.54
Athens was making a big pitch for a sell-off.

Faced with a disappointing response to the international tender
and confronted by mounting industrial unrest, the government, in
July 2001, announced its decision to start negotiations with its pre-
ferred bidder Axon Airlines, a small private Greek airline owned by
Thomas Liakounakos.55 The government’s hopes for a quick sale of
Olympic Airways were soon to be dashed by the events of 9/11 and
the subsequent global crisis that engulfed the airline industry. By
February 2002 negotiations had ended in failure, leaving the Greek
government in limbo. During the same period, pressure by the Com-
mission also began to mount. Following a series of complaints by
Olympic’s competitors, the Commission announced its intention to
launch a new investigation into state aid to Olympic and threatened
that the Greek flag-carrier might have to return to the government all
state aid authorized since the 1994 restructuring plan, worth in
excess of €1.5 billion.56 Amidst a period of high uncertainty for the
international aviation industry, the Commission appeared to have
lost faith with the Greek government and delivered a serious blow
to Olympic Airways. This was the beginning of a tense relation-
ship between the Greek transport minister and the transport
commissioner.

As relations with the Commission continued to deteriorate, the
government announced in February 2002 yet another plan for the
rescue of Olympic. Acknowledging that the potential suitors of
Olympic Airways were ‘too small’ to buy the entire OA group (includ-
ing all its subsidiaries), Verelis was now ready to accept a ‘salamis-
slicing’ strategy for the privatization of Olympic. According to the
plan the most profitable non-aviation subsidiaries of the OA group
would be sold separately to private investors. At the same time, all
aviation services performed by Olympic Airways and its subsidiaries
would be merged under one company and sold off. In order to entice
potential investors, the government also promised to terminate OA’s

54 Ta Nea, 7 December 2000.
loss-making route to Australia and absorb any staff that would not be
needed by the airline’s new owners.57

Under the threat of a new Commission investigation and the
possibility of being forced to return huge amounts of illegal state aid
to the Greek government, the interest of potential investors in the
purchase of Olympic was predictably limited and confined predomi-
nantly to a small group of Greek businessmen. In December 2002,
Golden Aviation, a consortium led by Greek shipping tycoon Stamatis
Restis, was announced as the government’s preferred candidate to
buy Olympic.58 The initial optimism, however, that a deal could be
finalized within two months was shattered following the publication,
in December 2002, of the Commission’s decision on state aid to
Olympic. In it, the Commission produced a damning report of the
handling of Olympic’s ‘restructuring’ since 1994 and focused, in
particular, on fresh allegations of state aid since 1998. The Commis-
sion’s decision concluded that the Greek government should recover
from Olympic the sum of €119 million that the airline received as aid
in the form of preferential tax treatment over the period 1998–2002
as well as €41 million that Olympic received in the summer of 1998 as
part of the second instalment of the 1994 rescue plan.59

The Greek minister of transport responded angrily to the Commis-
sion’s decision and accused De Palacio of trying to shut down Olympic
at a time when the Greek government was negotiating its sale.60 In an
attempt to keep the process of privatizing Olympic alive, Verelis
insisted that the Greek government would resist the Commission’s
decision all the way to the ECJ and that the new owners of the airline
would not be burdened with €160 million that the Commission had
asked OA to return to the Greek state. In the meantime, the airline
would continue to operate as normal.61 Despite Verelis’s protestations,
however, the cloud that the new Commission decision cast over the
future of OA had fatally undermined the negotiations between the
Greek government and Golden Aviation which, in February 2003,
announced it was no longer interested in buying Olympic.62

57 Eleftherotypia, 22 February 2002.
58 Ta Nea, 7 December 2002.
59 Commission of the European Communities, ‘Decision on Aid Granted by
60 Ta Nea, 12 December 2002.
With the OA privatization process in tatters and his relations with the Commission suffering a complete breakdown, Verelis announced that the Greek government would now seek to implement a SwissAir-like solution for Olympic. For this purpose, the minister proposed the creation of a new company, called Olympic Airlines, which would take over all aviation activities of Olympic Airways. The new airline would service the entire network of the ‘old’ Olympic, but it would be much smaller than its predecessor. It would employ a total of 1,850 staff (out of the 5,000 employed in the aviation side of the ‘old’ Olympic), all of which would have to sign new revised collective agreements with the new airline. These agreements would provide for salary cuts and a much tighter employment regime in the new airline and they were designed to replace the incredibly complex (and generous) network of 240 sectoral and ad hoc agreements signed between the union and the management of the ‘old’ Olympic. Crucially, Olympic Airlines would be free from all debts of the ‘old’ Olympic which, by the end of 2001, had reached €500 million. These debts, together with the staff that would not join the new airline, would remain in the ‘old’ Olympic (renamed Olympic Airways-Services) which would oversee an early retirement (or redeployment) scheme for excess personnel before eventually being closed down. The new plan also provided for the privatization of all subsidiaries of the Olympic Airways group, which, it was hoped, would generate enough proceeds in order to finance the OA’s early retirement scheme as well as the return of €194 million of illegal state aid from the old Olympic to the Greek government (if Greece lost the case in the ECJ).63

In the aftermath of Verelis’s announcements, the government came under a barrage of criticism from the OA unions. Despite the fact that the new plan made no reference to compulsory redundancies, the proposed salary cuts and job loses met huge opposition particularly from the pilots’ (EXPA) and the flight attendants’ (EISF) unions. The mathematics of the exercise were indeed challenging. The ‘old’ Olympic had a total of 649 pilots and 1,100 flight attendants whereas the new plan provided for 420 and 600 vacancies respectively. For their part, the unions were confronted with the dilemma of whether to accept the proposed job loses and encourage their members to opt for the early retirement scheme on offer or to resist

the changes to the bitter end. The minister of transport, on the other hand, was forced to choose his friends carefully. Having secured the agreement of the ground staff unions to join the new airline, Verelis knew full well that his experiment was doomed to failure if the pilots did not get on board. The cost of achieving this consent was an early retirement package worth €200,000 for each of the 140 pilots who opted to join the scheme. In addition, EXPA was promised that pilots would be given a share of the ‘new’ Olympic once the airline was privatized.

Verelis was far less generous to the flight attendants’ union. EISF had taken a rejectionist line, arguing that flight attendants had already accepted significant sacrifices during the 1990s and that they were entitled to a deal similar to that of the pilots. Verelis refused and EISF engaged in a 76-day strike. Under Verelis’s instructions, the management of OA moved quickly to recruit fixed-term contract staff to replace EISF’s striking members and keep Olympic operational. As the new law on Olympic Airlines passed through parliament in September 2003, the momentum of EISF’s strike began to dwindle. By the time the new Olympic Airlines had officially replaced Olympic Airways in December 2003 the majority of EISF’s members had agreed to transfer to the new airline, whilst 256 of them had opted for early retirement.

The birth of Olympic Airlines was greeted with enthusiasm by the minister of transport, who argued that the complex handover had gone smoothly. He insisted that the outcome of the 2003 reform was the best possible outcome under the circumstances. Faced with an exceptionally difficult period for international aviation and confronted with what he regarded as the disruptive influence of the Commission in the process of privatizing Olympic, the minister defended his legacy with vigour. The new Olympic Airlines, he argued, was a slimmer, more competitive and debt-free airline that would be more attractive to international investors. By separating Olympic Airlines from the ‘old’ Olympic, the liabilities of the Greek state and future investors were now clear and transparent. For his opponents, however, Verelis’s strategy had achieved little. Four years

64 60 more pilots agreed to be redeployed in the Civil Aviation Authority.
into his ministerial post, Olympic was still an entirely state-owned airline that continued to lose huge mounts of taxpayers’ money. Having failed to ‘offload’ Olympic from the Greek state, Verelis’s preoccupation during his last 18 months in the ministry had been how to avoid the airline collapsing and thus damaging his political career.

In any event, Verelis’s EU nemesis did not take long to arrive. In February 2005, the advocate general of the ECJ published his Opinion (C-415/03) on the Greek government’s appeal against the Commission’s 2002 decision. The advocate general agreed with the Commission’s assessment that the Greek government had indeed provided illegal state aid to Olympic Airways (worth €160 million) and that the creation of Olympic Airlines by the ‘Verelis law’ in 2003 ‘created legal and economic obstacles to the effective implementation’ of the Commission decision. In the final ruling of the ECJ published on 12 May 2005, the Advocate General’s reasoning was upheld in its entirety (OJ C182/10, 23.7.2005).

In the aftermath of the ECJ ruling, the future of Olympic came once again under severe threat. In the meantime, a new centre-right government won the April 2004 Greek elections and a new minister of transport, Mihalis Liapis, was given the task of dealing with the ‘hot potato’ of Olympic. Like his predecessor, Liapis soon announced that the government was committed to retreating from the management and ownership of Olympic and he called a new international tender for the sale of Olympic Airways/Airlines. However, in September 2005 a new Commission investigation concluded that Olympic Airlines and Olympic Airways-Services had received over €540 million of illegal state aid for the period 2002–5. With Olympic’s liabilities outweighing its assets by 5:1, the government had to concede that the closure of Olympic was now inevitable. In spring 2006, newspaper reports suggested that the government had agreed with private investors for the creation a new airline, Pantheon, in which the Greek state would hold a minority stake and no management rights. The new airline would operate some of Olympic’s routes and absorb a

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68 Kathimerini, 13 January 2005.
69 www.in.gr, 15 September 2005.
70 To Vima, 9 April 2006.
fragment of its staff, but would not carry any of the liabilities of OA, which would be declared bankrupt. Like many of its predecessors, the government appeared confident that, this time, the solution to the problems of Olympic would be for real. Time will tell whether such optimism is matched with events on the ground. In the short term, OA’s problems continue: Liapis felt obliged to sack Petros Papageorgiou in April 2006 as the company’s president, following the latter’s comment that OA should have been sold off even for one euro and his unprecedented failure to have any of his proposals accepted by the OA board.71

CONCLUSION

This has been a case study of non-compliance in the Europeanization process that raises questions of the interests, instruments and strategy of the Commission on the one hand, and the interests, capabilities and strategy of a member government, on the other. It is a different type of case from that considered in a number of other instances of ‘non-compliance’, however. It is not one of the transposition of EU directives, but rather of the Commission possessing executive authority in certain areas (state aids) and utilizing them across a broader agenda on which its direct competences are more limited (the form of restructuring, privatization). A critical dimension is of the member government straddling two arenas: negotiating package deals with the Commission and satisfying or ‘neutralizing’ domestic veto players. Moreover, the case is not one of stable positions and a test of compliance: both the Commission and the Greek government shifted their bargaining positions, to some degree, and the latter was not simply evading the prior instructions of the former. The agenda shifted, as solutions were tried and failed. Ministers in Athens showed themselves to be involved in a learning process: the options seen as feasible changed over time, not least in relation to the expectations of the Commission.

This has been a case, then, of a dynamic bargaining process leading to a conclusion that appears sub-optimal to both the Commission and the Greek government. The outcome is paradoxical. The Simitis government equated Europeanization with modernization

71 NET, 20 April 2006.
and could confidently expect the former to be a means to public legitimization for the latter. Entry into EMU had been matched by a new rhetoric of fiscal discipline. Though its internal divisions meant that reform initiatives had to be carefully crafted politically, the Simitis government in fact displayed a rational set of preferences on the future of Olympic. The essential interest was one of divestment of OA from the state and this was consistent with a range (and sequence) of solutions.\textsuperscript{72} The Commission, for its part, acted in line with the priority to eradicate state aids and promote a more competitive market. Athens and Brussels therefore seemed to pursue parallel strategies, albeit leading to breakdown and an ECJ clash. The fundamental question that arises from this result is: \textit{why}?

The concern here has been to trace how and why the conflict developed and to place this in the framework of compliance. The intent has not been to apportion praise or blame. The extent to which strategies and outcomes were determined by political cunning or ineptitude on the part of the Greek government is unclear. Both may have played a part. The context encouraged inventiveness by the government vis-à-vis the Commission when seeking solutions in a tightly constrained process.

The representation of bargaining positions in terms of win-sets highlights the key points. In 1994, the Commission and the Greek government had win-sets that partially overlapped with each other – both accepted the need for a rescue package for OA, both shared views about the need for OA to shift towards a more commercially-based operation – whilst the unions’ win-set also connected in so far as it embraced new financial aid. By the Verelis law of 2003, the win-sets of the Greek unions must be disaggregated as a result of the differential impacts on the employment contracts of the distinct groups of workers. Some marginally overlapped (ground staff, pilots) with that of the government; others did not (flight attendants). Crucially, however, by 2003, the win-set of the government barely touched that of the Commission.

\textsuperscript{72} The divestment strategy was consistent with an array of potential solutions: placing OA under a major foreign strategic partner, seeking a foreign purchaser, and creating a new company as part of a radical restructuring plan. Each were intended to bring to an end the continuing drain on the state posed by OA’s position; in that sense, they were indeed compatible with an end to state aids and the shift of OA to a fully commercial criteria of operation.
The relevance of the two hypotheses elaborated at the outset has been evident from the case study. The Commission and the Greek government veered away from each other, as a result of differences over the clarity and consistency of the signals each gave; the time horizons each operated within; and the credibility and trust each had with the other. A sub-optimal outcome appeared the result of a relationship between the EU Commission and the Greek government somewhat akin to a ‘paradox of cooperation’.\(^73\) Cooperation had broken down as both parties felt their interests were being challenged, rather than accommodated, and the incentives diverged. A story of compliance that began with a shared management of the problem (the 1994 package of measures), finished with an issue of enforcement and coercion (the ECJ case). The twinning of cooperative and coercive instruments by the Commission is more likely to succeed in achieving domestic compliance.\(^74\) In the area where it was most dependent on cooperation – the form and timing of restructuring – the Commission eventually shifted to confrontation. It settled for its veto power, rather than a proactive role in finding a workable solution in an area where it had little direct authority. Palacio’s liberalizing vigour had certainly accelerated this trajectory of conflict.

Yet, the domestic constraints faced by Greek ministers – entrenched union power, internal dissension within the government and an ambivalent public – provided strong incentives for them to seek solutions that tested the limits of what the Commission would accept. Whilst ministers remained uncertain as to what these limits would be, it was evident that strategy was being moulded by constraints imposed at home. The Greek government could not deliver a reform more acceptable to the Commission. Moreover, subsequent events have testified to the seemingly intractable nature of the problem: OA refuses to live or die.

The case suggests the relevance of two linked agendas of governance: the ability of the Commission to steer an EU-wide agenda of

\(^73\) Two sets of rational behaviour, shaped by distinct (though overlapping) institutional conditions, produced an outcome that both had worked hard to avoid (K. A. Shepsle and M. S. Bonchek, *Analyzing Politics: Rationality, Behavior, and Institutions*, London, W. W. Norton & Co., 1997, p. 204.


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economic reform, given its current policy instruments, and the capacity of a government like that of Greece to deliver on EU-level commitments. This is an agenda of increasing importance to an enlarging EU. Greece is a crucial test case that illustrates the nature of the problem at the heart of this shared governance.