NATO OTAN

NIAG

NATO INDUSTRIAL ADVISORY GROUP

HIGH LEVEL ADVICE STUDY NO 154

DEVELOPMENTS IN EUROPE TO REFORM EXPORT CONTROL AND DEFENSE PROCUREMENT PROCESSES

+

IMPLICATIONS AND OPPORTUNITIES RESULTING, PARTICULARLY WITH REGARD TO MULTINATIONAL PROGRAMS SUPPORTING NATO CAPABILITIES AND INTEROPERABILITY

SUMMARY

1. Executive summary 3

2. Background Info 5

a) EU Export Controls 5

1. Intra-EU transfers of defence products 5

2. Dual-use export controls in the EU 6

3. EU exports of military equipment to third countries 7

4. US-UK Defence Trade Cooperation Treaty 9

b) EU Defence and Security Procurement 9

c) EU activities on defence standards 15

5. LoI framework 15

3. Implications for NATO TADIC 16

4. Recommendations / questions for consideration 17

1. EXECUTIVE SUMMARY

This is the white paper for the NATO's 14 October 2011 Trans-Atlantic Defence Industrial Cooperation (TADIC) conference attendees on the developments in Europe to reform export control and defense procurement processes.

The European defence equipment market, worth €41 billion in 2009, is technology-intensive with cutting-edge research and development in fields such as electronics, ICT, transport, biotechnology and nanotechnology. Many new technologies developed for defence have also turned into drivers for growth in civil sectors such as in global positioning and earth observation.

The European defence industry is mostly concentrated in six Member States (France, Germany, Italy, Spain, Sweden and the UK) although companies producing ancillary equipment and systems are found all over Europe.

However, the European defence market is still highly regulated at a national level and fragmented. Europe's defence-related industries (primarily the defence part of sectors such as aeronautics, space, electronics, land systems and shipbuilding) largely operate outside the internal market. Member States have maintained national control over defence equipment markets and related industries with reference to Article 346 of the Treaty on the Functioning of the European Union (TFEU) which permits EU Member States to circumvent the common market by providing that "any Member State may take such measures as it considers necessary for the protection of the essential interests of its security which are connected with the production of or trade in arms, munitions and war material."

European governments have a clear preference for their own national defence industries not only to protect jobs and boost investment but also to ensure security of supply and of information. Some Member States are still reluctant to accept mutual dependence. As a consequence, producers from other Member States have only limited, or no, access to domestic defence markets. This fragmentation and divergent national policies creates red tape, hampers innovation and leads to duplication of defence programs and research. Ultimately this undermines competitiveness of the European Defence industry and the effectiveness of the European Common Security and Defence Policy (CSDP).

Nevertheless, the situation is now evolving. The economic pressure resulting from reduced defence budgets after the end of the cold war and the current crisis, and the escalating development costs, make the maintenance of a comprehensive national defence industrial base impossible for any single European state. The European defence industry has therefore to enhance its competitiveness as much as possible. The technological evolution towards multiple

use and bridging technologies is an important new challenge presenting opportunities and difficulties.

With this background, the European Commission launched a "Defence Package" on 5 December 2007 designed to set out a new European policy and legislative framework to improve the competitiveness of the European defence sector.

Following the European Commission's adoption of this "Defence Package", two directives were published in 2009 with a view to facilitate the development of a European defence equipment market: (a) Directive 2009/43/EC on intra-EU transfers of Defence products simplifying terms and conditions of transfers of defence-related products within the Community and (b) the 2009/81/EC Defence and Security Procurement Directive on the coordination of procedures for the award of certain works contracts, supply contracts and service contracts awarded by contracting authorities or entities in the fields of defence and security. The package also consists of the Communication "Strategy for a Stronger and More Competitive European defence Industry".

The 2009/81/EC Directive doesn't mention the term offset but it addresses the offset practices indirectly by providing for subcontracting, conditions on contract performance, and contract award criteria to inhibit the application of offsets.

Several other initiatives have been launched to overcome or mitigate challenges toward a more European defence market. Noteworthy efforts include key European Defence Agency initiatives (such as the Electronic Bulletin Board (EBB), the voluntary Code of Conduct on Offsets, the voluntary Code of Best Practice in the Supply Chain) and the European Committee for Standardisation (CEN)'s workshops on Standardisation for Defence Procurement.

This white paper yields following seven major recommendations for TADIC development:

a. Enlarge the transatlantic approved community within the TADIC export control framework

b. Define the scope of an essential security interest in Article 346 TFEU

c. Create more mutual transparency on defence planning

d. Limit the adverse impact, if any, of the new 2009/43/EC and 2009/81/EC Directives on the North American Industry

e. Limit the adverse impact of technology control policies

f. Promote mergers, acquisitions and joint ventures in the security and defence sector

g. In times of austerity, the EU and NATO should cooperate and seek for smart solutions.

2. BACKGROUND INFO

(http://ec.europa.eu/enterprise/sectors/defence/defence-industrial-policy/index_en.htm)

(http://www.eda.europa.eu/defencefacts/)

a) EU Export Controls

1. Intra-EU transfers of defence products

(http://ec.europa.eu/enterprise/sectors/defence/documents/)

Until recently, fragmentation of the European defence market and divergent national approaches caused many problems for the European defence industry. For example, national systems to control the transfer of defence equipment to another Member State did not distinguish between exports to third countries and transfers between Member States. Heterogeneous national licensing regimes hampered the security of supply between Member States. A study on "intra-community transfers of defence goods" from 2005 estimated costs raising from obstacles of intra-community transfers of €3.16 b per year (direct costs €434m, indirect costs €2.73 b per year).

The new Directive 2009/43/EC on intra-EU transfers of defence products, amended by Commission Directive 2010/80/EU of 22 November 2010, aims at alleviating these obstacles.

The Directive induces Member States to replace as far as possible their existing individual licences with general licences for those intra-Community transfers where the risk of re-exportation to third countries is under control, such as purchases by armed forces of other EU Member States and transfers to certified companies of components in the context of industrial cooperation.

Global licences, grouping multiple transfers to several recipients by one supplier, will cover most of the remaining intra-community transfers, with individual licensing thus becoming the exception. Member States will remain free to determine the products eligible for the different types of licence and to fix the terms and conditions of such licences.

Member States will have to transpose the Directive by 30 June 2011 at the latest. They will have to apply the Directive from 30 June 2012.

2. Dual-use export controls in the EU

(http://ec.europa.eu/trade/creating-opportunities/trade-topics/dual-use/index_en.htm)

The EU export control regime for dual-use goods and technologies is governed by Council Regulation (EC) No 428/2009 of 5 May 2009 setting up a Community regime for the control of exports, transfer, brokering and transit of dual-use items. The list of controlled dual-use items is set out in Annex I to Regulation 428/2009. Items not listed in Annex I may also be subject to export controls under certain conditions specified in the Regulation.

Under the EU regime, controlled items may not leave the EU customs territory without an export authorisation. Additional restrictions are also in place concerning the provision of brokering services with regard to dual-use items and concerning the transit of such items through the EU.

Dual-use items may be traded freely within the EU except for those listed in Annex IV to Regulation 428/2009, which are subject to prior authorisation.

Suppliers wishing to apply for authorisation have to contact their competent national authorities for details of what information must be supplied.

National authorities may require export controls on unlisted dual-use items (see Articles 4 & 8 of Regulation 428/2009). Exporters should therefore refer to their relevant national rules and check the situation with regard to their specific transactions.

Such ad-hoc controls may apply where there is a risk that an export to a specific end-user might be diverted for use in a weapon of mass destruction, in violation of an embargo or in certain other situations specified in the Regulation.

Individual EU countries may keep in place certain specific national rules. Such rules can apply to additional items to be controlled (Articles 4 & 8). They can require goods to be checked at specific border points (Article 17). They can introduce additional checks inside the EU (Article 11).

The EU list of controlled items is based on control lists adopted by international export control regimes – the Australia Group (AG), the Nuclear Suppliers Group (NSG), the Wassenaar Arrangement and the Missile Technology Control Regime (MTCR).

The European Commission is a member of the Australia Group and of the Nuclear Suppliers Group.

Candidate countries for EU membership, such as Turkey, Croatia and the Former Yugoslav Republic of Macedonia, are required to apply the EU regime, and the EU is actively promoting Croatia's membership in

all the regimes to which it is applying (Croatia is already member of Wassenaar and Nuclear Supplier's Group).

3. EU exports of military equipment to third countries

(http://www.consilium.europa.eu/showPage.aspx?id=1484&lang=en)

The EU export control policy is governed by Council Common Position 2008/944/CFSP of 8 December 2008 defining common rules governing control of exports of military technology and equipment to third countries.

In 1998 the Council adopted the European Union Code of Conduct on Arms Exports which set up eight criteria for the export of conventional arms, established a notification and consultation mechanism for denials and included a transparency procedure through the publication of the EU annual reports on arms exports. The Code contributed significantly to the harmonisation of national arms export control policies and its principles and criteria have been officially subscribed to by various third countries.

Common Position 2008/944/CFSP marked the formal successful conclusion of a review of the Code and set another milestone in improving the EU's export control standards. The Common Position constitutes a significantly updated and upgraded instrument which replaces the Code of Conduct. It includes several new elements, which deepen and widen the scope of application. These elements include the extension of controls to brokering, transit transactions and intangible transfers of technology, as well as the implementation of strengthened procedures in order to harmonise Member States' export policies. Recognizing the special responsibility of military technology and equipment exporting states, Member States continue to show determination to debate the export of military technology and equipment which might be used for undesirable purposes such as internal repression or international aggression or contribute to regional instability.

The Council assesses implementation of the Code on an annual basis. Article 8(2) of the EU Common Position provides for the publication of an EU Annual Report (see Eleventh Annual report on http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2009:265:FULL:EN:PDF).

According to this Eleventh Annual report of 6 November 2009, Member States have identified the following priority guidelines for the near future:

continuation of the process of earlier adoption and harmonization of national reports in order to promote more homogeneous statistical data for inclusion in the European Union annual reports, to produce clearer, transparent and complete summary tables;

(b) continuation of activities for the promotion of an Arms Trade Treaty;

(c) implementation of Common Position 2003/468/CFSP, taking into account different national legislation and expanding the appropriate information-sharing mechanism and transparency in reporting;

(d) continuation of the policy of promoting the principles and criteria of Common Position 2008/944/CFSP among third countries, especially those countries that have aligned themselves with the Common Position, and assisting its practical implementation through, inter alia, the provision of practical and technical assistance to ensure the harmonisation of policies on arms export control;

(e) expert contribution to discussions on the implementation of Directive 2009/43/EC;

(f) further development of dialogue with the European Parliament;

(g) continued close cooperation and consultation with the interested third parties, including international NGO's and the defence industry.

The 12th report is available on http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2011:009:0001:0417:EN:PDF

Article 12 of Common Position 2008/944/CFSP stipulates that the EU Common Military List shall act as a reference point for Member States' national military technology and equipment lists, but shall not directly replace them.

The EU Common Military List also serves as a basis for interpretation by Member States of all EU arms embargoes.

The "User's Guide to Council Common Position 2008/944/CFSP" (http://register.consilium.europa.eu/pdf/en/09/st09/st09241.en09.pdf), drawn up and regularly updated by the Working Party on Conventional Arms Exports (COARM), serves as guidance to assist Member States in implementing the Common Position (cf. Article 13 of the Common Position). It is intended for use primarily by export licensing officials

The User's Guide to the European Code of Conduct on Exports of Military Equipment, which is regularly reviewed, serves as guidance for the implementation of this Common Position.

4. US-UK Defence Trade Cooperation Treaty

This Treaty is a significant change to how US-UK exports are managed and will allow the movement and transfer of equipment and information between pre-approved US and UK government agencies and contractors (the "approved community") without ITAR export licenses. By doing so, it will improve interoperability between UK and US forces and support to operations and facilitate cooperation between their industries.

One of the aims is to improve the efficiency of defence procurement by permitting the US to trade many non-sensitive defence articles with Britain without an export licence.

"By simplifying export licensing arrangements for government end use, the treaty will facilitate the more rapid movement of equipment and information between the UK and the US whether purchased off-the-shelf, as part of bilateral project or in support of joint operations," UK's former Defence Minister Nick Harvey said.

The UK is proceeding to implement the Treaty over the course of the year 2011.

b) EU Defence and Security Procurement

(http://ec.europa.eu/internal_market/publicprocurement/dpp_en.htm)

The legislative framework for defence procurement in Europe is deficient:

(1) Uncertainties persist regarding the use of Article 296 of the Treaty (TEC), now Article 346 (TFEU), which allows Member States to derogate from European Community (EC) rules if this is necessary for the protection of their essential security interests.

(2) The Public Procurement Directive, even in its revised version (Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts), is generally considered ill-suited for many defence contracts.

Therefore, the European Commission chose to introduce specific rules for procurement in the defence sector. These rules would facilitate cross-border procurement of Member States. Up until

now, the vast majority of defence procurement contracts have been exempted from the rules of the Single Market on the basis of Article 346 (TFEU). This practice stands in contrast to the case law of the European Court of Justice and hampers the openness of defence markets between Member States. The same problem exists, albeit less prominently, for sensitive non-military security equipment. In order to improve this situation, the Commission adopted a new Directive, tailor-made for defence and security. Member States will soon have at their disposal Community rules they can apply to complex and sensitive procurements without putting at risk legitimate security interests.

Directive 2009/81/EC of the European Parliament and of the Council of 13 July 2009 coordinates the procedures for the award of certain works contracts, supply contracts and service contracts by contracting authorities or entities in the fields of defence and security and amends Directives 2004/17/EC and 2004/18/EC.

By 21 August 2011, Member States have to adopt and publish the laws, regulations and administrative provisions necessary to comply with this Directive. They shall forthwith communicate to the Commission the text of those measures.

By 21 August 2012, the Commission will have to report on the measures taken by Member States with a view to the transposition of this Directive, and in particular Article 21 and Articles 50 to 54 thereof.

The Commission will also have to review the implementation of this Directive and report thereon to the European Parliament and the Council by 21 August 2016. It shall evaluate in particular whether, and to what extent, the objectives of this Directive have been achieved with regard to the functioning of the internal market and the development of a European defence equipment market and a European Defence Technological and Industrial Base, having regard, inter alia, to the situation of small and medium-sized enterprises. Where appropriate, the report will have to be accompanied by a legislative proposal.

Directive 2009/81/EC sets Community procurement rules which are adapted to the specificities of the defence/security sectors. It allows, for example, the use of the negotiated procedure with publication as the standard procedure and provides special provisions for security of supply and security of information. The existence of this Directive will limit Member States' use of the exemption provided for in Article 346 of the Treaty on the Functioning of the European Union to exceptional cases, in line with Court of Justice rulings. Taking into account the increasingly blurred dividing line between security and defence, the new rules will also apply to sensitive contracts in the field of non-military security. This Directive is the logical follow-up to the Interpretative Communication on the application of Article 296 of the Treaty, which was adopted in December 2006 (IP/06/1703). This Communication clarifies the conditions for the use of Article 296 and

gives guidance to awarding authorities for their assessment of whether defence contracts can be exempted from Community rules or not.

The Communication is a non-legislative measure and does not modify the existing legal framework. It only concerns defence procurement by national authorities inside the EU and does not deal with defence contracts with third countries, which are managed on bi-lateral levels by each Member State.

Derogations under Article 346 (TFEU) are a politically and legally serious matter. The EU Treaty therefore contains strict conditions for the use of the exemption, balancing Member States' security interests with the principles and objectives of the Community. According to the Court of Justice, the use of the derogation must be limited to clearly defined and exceptional cases and interpreted in a restrictive way.

This means in particular that Article 346 (TFEU) does not provide for an automatic exemption of defence procurement in general. On the contrary, Member State must carefully carry out, for each procurement contract, a case-by-case assessment of whether the use of the exemption is legitimate, with respect to both the field and the conditions of application of Article 346 (TFEU). Only the protection of essential security interests justifies an exemption. Other interests connected with the production of or trade in defence equipment, in particular economic and industrial interests, are by themselves not sufficient to justify derogating from EU procurement rules. The security interests at stake must be "essential". This implies that possible exemptions are limited to defence procurement contracts which are of highest importance for Member States' military capabilities. It is the Member States' prerogative to define and protect their essential security interests, and to decide on which military equipment they want to procure. However, as guardian of the EU Treaty, the Commission may ask Member States to furnish evidence for the justification of the exemption of a procurement contract. It can also bring a matter directly before the Court if it considers that a Member State is making improper use of the powers provided for in Article 346 (TFEU). In this case, it is for the Member State to prove that the use of the exemption is necessary for the protection of its essential security interests.

In order to ensure correct transposition and application of Directive 2009/81/EC, the European Commission’s Director General (DG) Internal Market and Services developed guidance notes on the most important aspects of the Directive. These guidance notes are legally non-binding. Only the Court of Justice is competent to give a legally binding interpretation of EU law. During the drafting process, several workshops were organised to discuss these guidance notes with Member States. On the basis of these discussions, a broad consensus was achieved on most issues. DG Internal Market and Services is nevertheless solely responsible for the content. Besides publishing guidance notes on (a) the field of application, (b) the exclusions, (c) security of information and (d) research and development, following topics are being discussed:

Security of Supply

The Directive recognises the particular importance of Security of Supply for defence and security procurement. Security of Supply is crucial, particularly in times of crisis, when reliable and in-time delivery can literally be vital. Moreover, Security of Supply is particularly challenging, because of the extremely long life-cycle of most military equipment, which necessitates logistical support, upgrades, modernisation etc for many years.

Subcontracting

Articles 21 and Title III (Articles 50-53) of the Directive contain provisions allowing contracting authorities/entities to require successful tenderers to subcontract a certain share of the main contract and/or to put proposed subcontracts into competition. Contracting authorities/entities may use these provisions to open the supply chain of successful tenderers to EU-wide competition, but they may not impose local suppliers as sub-contractors.

Offsets

Whether they are civil or military, direct or indirect in nature, and whatever their legal connection with the main contract is, offset requirements are restrictive measures which go against the basic principles of the Treaty, because they discriminate against economic operators, goods and services from other Member States and impede the free movement of goods and services. Since they violate basic rules and principles of primary EU law, the Directive cannot allow, tolerate or regulate them.

Article 4 of the Directive sets out the basic principle of non-discrimination of candidates and tenderers in contract award procedures: 'Contracting authorities/entities shall treat economic operators equally and in a non-discriminatory manner and shall act in a transparent way.' This principle prohibits all measures which imply a discrimination against participants in a procedure, for instance, by providing compensation obligations only for tenderers from abroad. This prohibition also covers discrimination targeting tenderers' supply chains (Article 21 (1)).

According to the Interpretative Communication, indirect non-military offsets are in general not covered by Article 346 (TFEU), since the latter Article protects only security interests and must be interpreted in a restrictive way. This means that civil offsets must respect Community rules even if they are related to a defence procurement contract which is exempted on the basis of Article 346 (TFEU). Moreover, the Interpretative Communication recalls that Member States must make sure that possible offset arrangements do not adversely affect competition on markets for non-military products.

The Interpretative Communication aims at better complying with EU law and greater openness of defence markets between EU Member States. It specifies the conditions and the field of application of the exemption provided by Article 346 (TFEU). Thus, it helps to distinguish between defence procurement contracts to which the Public Procurement Directive applies and those which can be exempted from Community rules on the basis of Article 296.

On 1 July 2009, a Code of Conduct (CoC) on Offsets administered by the European Defence Agency (EDA) came into effect (http://www.eda.europa.eu/newsitem.aspx?id=420). This Code is a voluntary, non-legally binding intergovernmental instrument, which sets out overarching principles and guidelines for the use of offsets in defence procurement. 25 Member States plus Norway signed up to the Code. The two instruments differ therefore in nature and purpose. At the same time, they are complementary, since the Communication indicates which contracts fall into the scope of the Code.

Both in its introduction and principles, the Code stipulates that its provisions have to be implemented within the framework of EU law. Moreover, the Code is part of the Intergovernmental Regime on Defence Procurement to which participating Member States subscribed 'without prejudice to their rights and obligations under the Treaties.' However, it is important to note that the application of the Code does not of itself make offset requirements compatible with EU law. In every award procedure, contracting authorities/entities first have to ensure that all their requirements comply with the provisions of the Treaty and/or the Directive. On that basis, they may then decide to apply the Code on offsets, provided that this does not put the award procedure in conflict with the Treaty and/or the Directive. In other words: The only legal criterion for the assessment of offset requirements is compliance with EU primary and secondary law.

It is clear that the European Commission and the EDA don't share the same view. So far European governments have been using two different approaches to liberalize the defense market: one based on law, with the European Commission; and the other based on pragmatic arrangements, centered around the EDA. There is also plenty of evidence that some European defense ministries are still reluctant to open up their defense procurement to more competition.

The Electronic Bulletin Board (EBB), operated by the EDA, is an important tool that allows for transparency and fair and equal opportunities to the suppliers as well as a mean for the EDA to monitor its application.

The EBB main objectives are:

To advertise sMS alll relevant new defence procurement opportunities which fall under the CoC
To assist suppliers in finding contracting opportunities and procurement details from sMS

To help EDA in the Reporting & Monitoring of the CoC

The EDA also developed a Code of Best Practice in the Supply Chain (hereinafter referred to as the "CoBPSC"). It is a voluntary Code for use where Article 296 of the TEC is invoked and the voluntary regime applies (other than for excepted goods and services). It is to be read and implemented coherently with the Code of Conduct, of which the CoBPSC is an integral part.

Many European defence industry associations conclude that offsets should be dealt with on an intergovernmental level through the EDA. Offsets, they say, deal with aspects closely related to national sovereignty and therefore the question of offsets in its entirety is not within the European Commission's purview. They encourage the EC not to promote the Guidance Note on Offsets and to support the important work of the EDA on offsets.

According to the EC's Directorate General Internal Market and Services, Member States have the right to define and protect their essential interests of security. Article 346 TFEU, therefore, provides for a derogation which allows Member States to take measures which they consider necessary for the protection of these interests. The EC doesn't exclude that certain offset requirements may be justified on the basis of this derogation. However, Article 346 by no means provides a blank check for offsets. As the EC explained in its Interpretative Communication of December 2006, the use of Article 346 is subject to a number of conditions and has to be interpreted restrictively. It must be limited to exceptional and clearly defined cases, and economic considerations are not accepted as grounds for justifying the derogation. Member States which intend to rely on it must assess and, if necessary, justify case by case whether the conditions for the use of Article 346 are fulfilled. This is the case also when Article 346 is invoked for offset requirements. This means that both EU primary and secondary law contain clear limits to offset requirements. As Guardian of the Treaties, the EC has the duty to ensure compliance with these limits. Consequently, the EC cannot agree with certain European defence industry associations' statement that "the question of offsets in its entirety is not in the Commission's purview [and] should be dealt with on an intergovernmental level through the EDA". In any case, offsets give priority to nationality over competitiveness. From an internal market perspective, they therefore constitute an economically questionable and legally unacceptable market distortion. In this context, the EC draws the attention to the Directive's provisions on security of supply and subcontracting. These provisions take into account all security-related arguments which Member States have put forward during the negotiation of the Directive to justify offsets. The provisions on security of supply, for example, make it possible to secure supply chains. The provisions on sub-contracting enable contracting authorities to drive competition into the supply chain of main contractors and will thus create EU-wide new business opportunities for sub-suppliers. This offers a legally correct and economically sound alternative to traditional offset practices.

c) EU activities on defence standards

Standardization of defence equipment is an important basis for the opening-up of national markets and the gradual creation of a single European defence market. In the framework of a project called "CEN Workshop 10 on Standardisation for Defence Procurement", managed by the European Committee for Standardisation (CEN) and sponsored by the European Commission, a European Handbook for Defence Procurement (EHDP) is being produced which contains references to standards and standard-like specifications commonly used to support defence procurement contracts, as well as guidance on the selection of standards and standard-like specifications to optimise effectiveness, efficiency, and interoperability (http://www.defense-handbook.org/). The Handbook's primary objective is to provide Defence Procurement managers with the 'state of the art' standards references supported by information on best practice when specifying them in defence contracts. It is also designed to complement the work of NATO in this area and the EDA. The Handbook has started its third and final phase of development. Work will probably be complete in summer 2011.

LoI framework

In July 2000, the six Letter of Intent (LOI) partners (France, Germany, Italy, Spain, Sweden, UK). signed a Framework Agreement covering (1) Security of Supply, (2) Transfer and Export Procedures, (3) Security of Classified Information, (4) Research and Technology, (5) Treatment of Technical Information and (6) Harmonization of Military Requirements. In these six areas, the partners committed themselves to create a more homogenous regulatory framework in order to improve market conditions for an increasingly transnational industry.

During a Spanish EU Presidency's workshop on February 15th, 2010, the Chairman of the Letter of Intent Executive Committee said:

"Under a LoI umbrella national experts worked closely together during 2008 and 2009 to establish common positions towards the Commission's draft Defence Procurement Directive. The working group was able to give advice to Commission on a number of key issues. This might be a model for dealing with any future activities being considered by the Commission in defence related matters. Leveling the playing field is one of the main objectives of LoI, as it is for the EDA. Participating Member States recognised an obvious need, as stated in the Joint Action, to "develop close working relations" between EDA and LoI. Of course a duplication of work should be avoided and relevant principles and practices of LoI could be assimilated or incorporated into EDA, as appropriate. Of course, developing the European Defence Technological and Industrial Base will

remain the core objective of LoI. But we might give also considerations to transatlantic defence industrial matters."

3. IMPLICATIONS FOR NATO TADIC

Legal

The EU Defence and Security Procurement directive considerably improves the current fragmented regulatory framework for defence procurement. It also significantly improves legal clarity. Awarding authorities will be able to assess which legislation to apply and justify their decision if necessary. This will improve legal certainty for all parties.

Administrative

Possible negative impacts will be low both for industry and for awarding authorities. In the medium to long term, greater transparency will certainly reduce administrative costs for companies, in particular Small and Medium-sized Enterprises (SME).

Economic

These depend considerably on the EU Defence and Security Procurement directive's acceptance by awarding authorities. This acceptance will certainly evolve over time. Initially, the directive may impact mainly on off-the-shelf procurement and technologically less sophisticated equipment. Greater openness of markets should enhance companies' chances to win cross-border contracts, thereby allowing the most competitive European companies to achieve economies of scale. The reduction of unit costs will then make their products more competitive on the global market. On the other hand, contracting authorities will obtain better value for money.

International

The introduction of EC procurement rules for defence and sensitive security will not change the situation regarding arms trade with third countries. Awarding authorities will continue to be able to invite to tender only EU companies or non-EU firms as well.

The UK-US Defence Trade Cooperation Treaty offers privileges to British entities only. The danger is that such a restriction could lead to a two-tier European defence market with non-British companies lagging behind.

The Directive 2009/43/EC ensures an EU-wide security of supply.

Operational

When European contracting authorities/entities will award a contract to the most economically advantageous tender, the criteria on which these contracting authorities/entities will base the award will not only be quality, price, technical merit, functional characteristics, environmental characteristics, running costs, lifecycle costs, cost-effectiveness, after-sales service and technical assistance, delivery date and delivery period or period of completion, operational characteristics, but also security of supply and interoperability which will improve the operational capabilities of the different Armed Forces.

After national certification in the scope of the ICT Directive, companies dealing in Europe with non-ITAR/EAR-controlled goods and technology can obtain general and global licenses instead of individual licenses and become part of a trusted community within the EU. However, companies, transferring ITAR/EAR-controlled items might loose the benefits of this ICT Directive because they still have to comply with US Government export regulations.

Transparency

The transparency will increase due to the obligation to publicize in the EU Official Journal.

The Commission will review the implementation of these Directives and report thereon to the European Parliament.

4. RECOMMENDATIONS / QUESTIONS FOR CONSIDERATION

Enlarge the transatlantic approved community

The UK-US Treaty should be enlarged to all EU Governments. At least the EU-based companies, "certified" according to Directive 2009/43/EC, could become part of a transatlantic "approved" community.

Define the scope of an "essential security interest" in Article 346 TFEU

The legally acceptable interpretations of an "essential security interest" should be defined in Article 346 TFEU in order to avoid that EU Member States consider Article 346 as an automatic exemption. A progressive opening of the market with improved security of supply between EU Member States and suitable procurement rules applicable throughout the EU might increase transparency and could also reduce the need to use these exemptions to the rules.

Create more mutual transparency on defence planning

EU Member States should provide each other more mutual transparency on their medium to long-term defence planning, which would allow opportunities to be identified for harmonised military requirements, joint investment projects, pooled acquisitions and coherent role specialisation. The EDA could play an important role here.

Limit the adverse impact, if any, of the new EU ICT and Defence Procurement directives on the North American Industry

According to DG Enterprise and Industry, Aerospace Industries, GMES, Security & Defence's Report on "The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries", the new ICT Directive provides Europe with a real leverage towards the US. The advantages offered by the new ICT Directive coupled with the EU Defence Procurement Directive provisions on security of supply are worrying to US industry, which fears it may be used to exclude it from European RFPs. This American concern provides important leverage for transatlantic negotiation, which is all the more important now, as ICT implementation details are being put in place. As a consequence the main recommendation of the study would be to move towards the establishment of transatlantic general licences for transfers to certified companies with the objective of promoting a greater predictability, transparency and efficiency of a transatlantic defence trade control regulatory framework. Those transatlantic general licenses would target specific European end-users approved by the USG.

With regard to offsets, being considered by some as "economically inefficient and trade distorting," the European Commission, the European Defence Agency, the European Member States, the US Government and the Canadian Government should consult regularly on a bilateral and multilateral basis in order to limit the adverse effects of offsets in defense procurement. Both sides of the Atlantic should benefit from a level playing field and maximum flexibility in competing for new security and defence procurements by shifting the paradigm from a national / European … defense industrial policy toward a transatlantic defence industrial policy among a community of trusted friends and allies.

Limit adverse impact of technology control policy

The technology control policy's abusive restrictions should be considered by industry on both sides of the Atlantic as the main inhibiter to trans-Atlantic defense industrial cooperation.

Foreign investment in the defence and security industrial base

In order to allow European and North American companies to "buy" into each other's foreign security and defence markets through mergers, acquisitions and joint ventures, restrictions on foreign investment in these markets should be avoided on both sides of the Atlantic.

In times of austerity EU and NATO should seek for smart solutions

Given the economic downturn, the EU and NATO Allies need to be realistic about what national and EU/NATO budgets will allow. Doing more with less means more efforts from the EU and NATO in specific areas, such as:

Pooling resources among groups of nations to increase economies of scale and reduce acquisition, operating, maintenance and training costs.
Many past successful efforts involved a small group of Allies pooling resources to acquire technologically mature capabilities (such as the C-17 initiative).
Participation by a larger number of Allies would, however, enhance the efficiencies and effectiveness of these pooling arrangements and reduce costs for all participants. A larger Ally could play a leadership role.
Multinational formations for maritime and air as well as land forces can be expanded. Multinational formations are often most practical among geographically proximate Allies, but should be considered wherever they afford members the opportunity to economize on current support resources, training, basing and other overhead costs. This can be especially helpful for smaller militaries in need of pooled combat multiplier assets such as higher level intelligence, engineering, transport, communications and fire support.
Role specialization: Larger nations could provide more high-end capabilities such as fighter aircraft, upper layer ballistic missile defense interceptors and sensors, and power projection from the sea. This would free smaller nations to focus on improving small unit deployability and effectiveness, particularly in specialties such as electronic warfare, civil affairs, counter-WMD, engineering, military intelligence, military police and units designed to conduct military and police training. Role specialization should not, however, provide a rationale for nations not joining pooling arrangements or not contributing capabilities in areas where we all should do more.
Better prioritization, eliminating expenditures on requirements that are less important and avoiding duplication, including between NATO and the EU. Greater efficiency will also be served by joint standards, training, and exercises for NATO and the EU, whether military, civilian, or civil-military.