

Towards a Coherent European Defence Procurement Regime?

European Defence Agency and European Commission Initiatives

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1. Introduction

The regulation of defence procurement in Europe is generally considered as requiring improvement,¹ and a number of initiatives have been taken on this issue over the past years. Especially, the European Union (EU) Member States created in 2004 a European Defence Agency (EDA) that was tasked, among other things, to make proposals for an intergovernmental regime that would apply to the procurement arms, munitions and war material. In parallel, the Commission of the European Community (EC) took a number of initiatives to clarify EC law on the matter.

However, such efforts have to be complementary, not competitive, and to finally achieve a seamless legal regime. This article will present the current status of the development of the EDA intergovernmental regime for defence procurement and of the European Commission's initiatives, and examine both for completeness and coherence.

2. Context of Defence Procurement in the EU

Defence procurement plays an important economic role in the EU. Defence expenditures of EU Member States amounted in 2005 to €193 billion, or 1.8% of the EU Gross Domestic

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¹ See e.g. Commission Green Paper on Defence procurement, COM(2004) 608 final, 23 September 2004; Trybus M., *European Defence Procurement Law – International and National Procurement Systems as Models for a Liberalised Defence Procurement Market in Europe* (Kluwer Law International, 1999); Heuninckx B., 'Defence Procurement in the EU: Time to Listen to the Wake-up Calls' (2006) 7(2) BLI 208; Georgopoulos A., 'Defence Procurement and EU Law', (2005) 30 EL Rev 559; Schmitt B. (rapporteur), 'Defence Procurement in the European Union – The Current Debate', Task Force Report, EU Institute for Security Studies, May 2005; Trybus M., 'Defence Procurement: The New Public Sector Directive and Beyond', (2004) 13(4) PPLR 198; Wheaton J. B., 'Defence Procurement and the European Community: The Legal Provisions', (1992) 1(6) PPLR 432

Product (GDP).² Of that total amount, about 18.3% (€35.4 billion) were used for the procurement of defence equipment and research and development activities, and about 26% (€50.3 billion) for operations and maintenance, as shown on Figure 1.

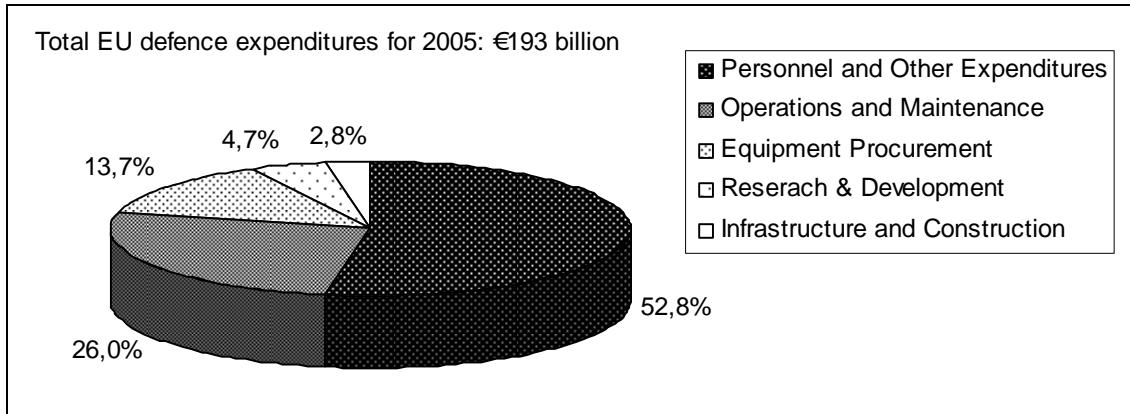


Figure 1: EU Defence Expenditures in 2005³

Even though defence procurement generally has to comply with the Treaty establishing the European Community (EC Treaty)⁴ and the related secondary legislation, in particular the Public Sector Directive,⁵ it can be subject to a number of exemptions for reasons of public security, especially Art.296 EC. A recent study has concluded that more than 50% of defence procurement in the EU was done outside the framework of the EC rules on public procurement because of that exemption.⁶ Article 296 EC states, in relevant part:

“(1)(b) 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; such measures shall not

² European Defence Agency, ‘European Defence Expenditures in 2005’, 20 November 2006, pp.1-4 – all these figures except Denmark; see also Kuechle H., ‘The cost of non-Europe in the area of security and defence’, European Parliament, DG External Policies, DGExPo/B/PolDep/2005/13, 19 June 2006, §1

³ European Defence Agency, ‘European Defence Expenditures in 2005’, above fn.2 – As the operations and maintenance figures for Belgium, Germany and Poland were not included in the EDA study, the original operations and maintenance expenditures have been increased by 20%, which corresponds to the percentage of total European defence expenditures for these three countries

⁴ Consolidated Version of the Treaty Establishing the European Community (EC Treaty), OJ 2002 C 325/33

⁵ 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, OJ 2004 L134/114, Art.10

⁶ European Defence Agency Press Release, ‘EU Governments Agree Voluntary Code for Cross-Border Competition in Defence Equipment Market’, Brussels, 21 November 2005; European Defence Agency Press Release, ‘EDA Welcomes European Commission Move on Defence Procurement Rules’, Brussels, 6 December 2005

adversely affect the conditions of competition in the common market regarding products which are not intended for specifically military purposes”.

These provisions apply to products included in a list drawn-up by the Council of the EC in 1958,⁷ which generally covers all ‘warlike’ or ‘hard’ defence material, but remains very general, thereby allowing diverging interpretations.⁸

In answer to arguments raised by the EC Member States arguing that ‘hard’ defence material was automatically excluded from the scope of the EC Treaty,⁹ the Court of Justice of the EC (ECJ) confirmed that Art.296 deals with clearly defined and exceptional cases and does not lend itself to any wide interpretation.¹⁰ Moreover, it does not create a general or automatic exemption,¹¹ and a Member State seeking to rely on Art.296 must provide evidence that it does not go beyond the limits of what is necessary for the protection of the essential interests of its security.¹² EC Member States have a certain degree of discretion when adopting measures that they consider necessary to guarantee public security but, in the circumstances of the case, the measures taken must in fact have the purpose of guaranteeing public security and be appropriate and necessary to achieve that aim.¹³

⁷ EC Treaty, above fn.4, Article 296(2); Council Decision 298/58 of 15 April 1958 on the list of products to which Article 223(1)(b) [now 296(1)(b)] EC Treaty applies (not published); the list was most recently published in Trybus M., ‘The List of Hard Defence Products under Article 296 EC’ (2003) 12(3) PPLR NA15; Written Question E-1324/01 by Bart Staes (Verts/ALE) to the Council, OJ 2001 C 364E/85

⁸ M. Trybus, *European Defence Procurement Law*, above fn.1, p.94; Eikenberg K., ‘Article 296 (ex 223) EC and External Trade in Strategic Goods’, (2000) 25 EL Rev 116, p.129

⁹ Trybus M., ‘Procurement for the Armed Forces: Balancing Security and the Internal Market’, 27 EL Rev 692, 2002, p.696; Wheaton J. B., ‘Defence Procurement and the European Community: The Legal Provisions’, above fn.1; Georgopoulos A., *European Defence Procurement Integration: Proposals for Action within the European Union*, PhD thesis, University of Nottingham, 2004, p.82

¹⁰ Case C-414/97, *Commission v Spain* [1999] ECR I-5585, at [21]; Case 222/84, *Marguerite Johnston v Chief Constable of the Royal Ulster Constabulary* [1986] ECR 1651, at [26]

¹¹ Case 222/84, *Johnston*, above fn.10, at [26]; Case C-273/97, *Angela Maria Sirdar v The Army Board and Secretary of State for Defence* [1999] ECR I-7403, at [16]; Case C-285/98, *Tanja Kreil v Bundesrepublik Deutschland* [2000] ECR I-69, at [16]; see also Rapp B. ‘Defence Procurement and Internal Market’, Institut für Strategie- Politik- Sicherheits- und Wirtschaftsberatung, Berlin, no date

¹² Case C-414/97, *Commission v Spain*, above fn.10, at [22]; for an analysis of the case, see Trybus M., ‘The Recent Judgment in *Commission v. Spain* and the Procurement of Hard Defence Material’ (2000) 9(4) PPLR NA99 and Trybus M., ‘Case Comment: On the Application of the EC Treaty to Armaments’ (2000) 25 EL Rev 663; Mezzadri S., ‘L’ouverture des Marchés de la Défense: Enjeux et Modalités’, Occasional Paper No 12, Institute for Security Studies, WEU, February 2000, p.8

¹³ Case C-273/97, *Sirdar*, above fn.11., at [27]-[28]; Case C-285/98, *Kreil*, above fn.11, at [24]-[25]

The Art.296 EC exemption cannot apply to activities relating to products not listed in the 1958 list.¹⁴ This does not specifically exclude dual-use goods from application of the exemption, but requires that the common market for their civilian applications not be affected by the use of the exemption.¹⁵

However, despite these rulings, the conditions under which the Art.296 EC exemption may be invoked are still not entirely clear and subject to debate.¹⁶

If, on the basis of these rulings, the Art.296 EC exemption is successfully invoked, it then has a general effect affecting all the EC Treaty provisions.¹⁷ This means that, in that case, defence procurement activities would not be subject to EC rules, and would follow applicable national procurement regimes, if any.¹⁸ Contracting authorities in the field of defence would be free, for instance, to award contracts to national firms without competition or advertising. In the name of the essential interests of the EC Member States' security, the latter has been the general rule for the procurement of arms, munitions and war material for a long time, often actually for purely protectionist reasons.¹⁹

¹⁴ Case T-26/01, *Fiocchi munizioni SpA v Commission*, [2003] ECR II-3951, at [61]-[64]

¹⁵ For instance, the District Court of The Hague, in its ruling no. 93/146 of 26 February 1993 in *Construccionen Aeronauticas SA (Casa) v Netherlands*, decided that Article 223 (now Article 296) could be invoked on the basis of the 1958 list for the procurement of transport aircraft for military purpose when the planes had to be significantly adapted for military use: see Jestaedt T., Derenne J., Ottervanger T., 'Study on the Enforcement of State Aid Law at National Level', European Commission, March 2006, p.373; see also the discussion in the recent Advocate General's Opinion in Case C-337/05 *Commission v Italy*, opinion of July 10, 2007, not yet reported, at [58]-[61]

¹⁶ See further Wheaton J. B., 'Defence Procurement and the European Community: The Legal Provisions' above fn.1; Eikenberg K., 'Article 296 (ex 223) EC and External Trade in Strategic Goods', above fn.8; Trybus M., 'Case Comment: On the Application of the EC Treaty to Armaments', above fn.12; Trybus M., 'Procurement for the Armed Forces: Balancing Security and the Internal Market', above fn.9; COM(2004) 608, above fn.1, §3.1; Georgopoulos A., 'Defence Procurement and EU Law', above fn.1; Schmitt B. (rapporteur), 'Defence Procurement in the European Union – The Current Debate', above fn.1

¹⁷ Case T-26/01, *Fiocchi munizioni*, above fn.14, at [58]-[59]

¹⁸ Communication from the Commission to the Council and the European Parliament on the results of the consultation launched by the Green Paper on Defence Procurement and on the future Commission initiatives, COM(2005) 626, 6 December 2005, p.3

¹⁹ Wheaton J. B., 'Defence Procurement and the European Community: The Legal Provisions', above fn.1; Communication from the Commission: 'The Challenges Facing the European Defence-Related Industry, a Contribution for Action at the European Level', COM(96) 10 final, 24 January 1996, §3.1.1, p.14; Trybus M., 'Procurement for the Armed Forces: Balancing Security and the Internal Market', above fn.9, at p.696; Schmitt B. (Ed.), 'European Armaments Cooperation – Core Documents', Chaillot Paper No 59, Institute for Security Studies, European Union, Paris, 2003, p.10; Valasek T., 'EU Wants More Defence Competition, Lower Costs', ISN Security Watch, Brussels, 1 December 2005; Kuechle H., 'The cost of non-Europe in the area of security and defence', above fn.2, pp.42 et.seq.

However, this attitude led to a heavily segmented and inefficient European defence equipment market, with numerous duplications of capacity across the EU Member States.²⁰ Studies have shown that 10 to 17% of the European defence procurement budget could be saved by centralising procurement and opening-up the defence equipment market.²¹ Some other studies argue that even up to 32% of the budget could be saved by a combination of reduced market fragmentation, increased efficiency of collaborative procurement programmes and harmonisation of requirements.²² Fortunately for the European taxpayer, EU Member States did not remain entirely insensitive to such figures.

3. The European Defence Agency

There had been for a long time talks about the creation of a centralised European defence procurement agency.²³ However, when finally deciding on the issue during the drafting of the EU Constitutional Treaty, the Council did not want to duplicate the multiple defence procurement agencies existing in Europe, and decided to create an agency with broader – but shallower – powers: a European Defence Agency (EDA).²⁴

However, as the ratification of the Constitutional Treaty was seemingly not progressing at a sufficient pace,²⁵ the Council created the EDA within the scope of the Common Foreign and

²⁰ Schmitt B., 'From Cooperation to Integration: Defence and Aerospace Industries in Europe', Chaillot Paper No 40, Institute for Security Study, WEU, July 2000, pp.79-83; Georgopoulos A., 'Defence Procurement and EU Law', above fn.1, at 567; Communication from the Commission: 'European defence – industrial and market issues – Towards an EU Defence Equipment Policy', COM(2003) 113, 11 March 2003, p.6

²¹ Mawdsley J., Quille G. et.al., 'Equipping the Rapid Reaction Force – Options for and Constraints on a European Defence Equipment Strategy', Paper 33, Bonn International Centre for Conversion (BICC), 2003, p.21, quoting Hartley K., 'The Common European Security and Defence Policy: An Economic Perspective', University of York, 2001

²² Unisys study, 'Intra-Community Transfers of Defence Products', Brussels, February 2005, §6.7

²³ Declaration (No 31) on Western European Union Annexed to the Final Act of the Maastricht Treaty, OJ 1992 C 191/1, at [5]; Cox A., 'The Future of European Defence Policy: The Case for a Centralised Procurement Agency', (1994) 3(2) PPLR 65; Hayward K., 'Towards a European Weapons Procurement Process – The shaping of common European requirements for new arms programmes', Chaillot Paper No 27, Institute for Security Study, WEU, June 1997; Cornu C., 'Fortress Europe – real or virtual?', in Schmitt B. (Ed.), 'Between cooperation and competition: the transatlantic defence market', Chaillot Paper No 44, Institute for Security Studies, WEU, January 2001, p.83, citing an initiative dating from 1978; COM(2003) 113, above fn.20, p.17

²⁴ Treaty Establishing a Constitution for Europe, OJ 2004 C 310/1, Articles I-41(3) and III-311 (which never entered into force); see also European Convention, Final report of Working Group VIII – Defence, CONV 461/02, 16 December 2002, at [64]-[65]

²⁵ Georgopoulos A., 'The New European Defence Agency: Major Development or Fig Leaf', (2005) 14(2) PPLR 103, p.109

Security Policy of the EU Treaty (CFSP).²⁶ The mission of the Agency is to support the Council and the Member States in their effort to improve the EU defence capabilities in the field of crisis management and to sustain the European Security and Defence Policy (ESDP).²⁷ To that end, its responsibilities cover capabilities development, armaments cooperation, defence industry strengthening, and research and technology.²⁸ All EU Member States, except Denmark, participate in the EDA²⁹ and are referred to as ‘participating Member States’ (pMS). However, the views of the EU Member States on the actual EDA role can vary widely: some consider it simply as a ‘registering body’ (especially the UK), while others would like it to take a broader role of ‘co-ordinating body’.³⁰

One of the concrete actions quite swiftly taken by the EDA has been the adoption of a voluntary and non-binding intergovernmental regime for defence procurement activities to which the Art.296 EC exemption applies (‘hard’ defence procurement). This regime includes a Code of Conduct on defence procurement, a Code of Best Practice in the supply chain, both supported by an Electronic Bulletin Board (EBB), a framework arrangement for security of supply, and provisions on security of information.³¹ Each of these will be discussed in turn in the following section.

4. Elements of the EDA Procurement Regime

4.1. Code of Conduct on Defence Procurement

In order to increase transparency on the part of participating Member States on the extent and nature of use of Art.296 EC in defence procurement, and to assess whether or not to proceed with a specific regime for ‘hard’ defence procurement, the EDA collected data from

²⁶ Council Joint Action 2004/551/CFSP of 12 July 2004 on the establishment of the European Defence Agency, OJ 2004 L245/17

²⁷ Ibid, Article 2

²⁸ Ibid, Article 5; see also Unisys study, ‘Intra-Community Transfers of Defence Products’, above fn.22, §3.2.5; Georgopoulos A., ‘The New European Defence Agency: Major Development or Fig Leaf’, above fn.25; Schmitt B., ‘The European Union and Armaments – Getting a Bigger Bang for the Euro’, Chaillot Paper No 63, Institute for Security Studies, European Union, Paris, 2003, on pp.40 et.seq., actually submitted a blueprint for the work of a European Armaments, Research and Capability Agency (ARCA) that is eerily similar to the current structure and working of the EDA

²⁹ Council Joint Action 2004/551/CFSP, above fn.26, Recital 21

³⁰ Kuechle H., ‘The cost of non-Europe in the area of security and defence’, above fn.2, p.39

³¹ For a description of this regime, see European Defence Agency, *A guide to the EDA’s new European Defence Equipment Market*, EDA, Brussels, 2007

participating Member States on the invocation (and non-invocation) of Art.296 EC.³² Although this data was unfortunately not published, the EDA concluded, as we stated above, that more than 50% of defence procurement by EU governments was done outside the framework of the EC rules on public procurement because of the exemption.³³

Therefore, the Agency proposed a voluntary Code of Conduct to increase cross-border competition in the European defence equipment market in the cases when the EC Treaty would not apply.³⁴ This Code of Conduct was approved by the EDA Steering Board on 21 November 2005 and took effect on 1 July 2006.³⁵

The EDA Code of Conduct on defence procurement defines the intergovernmental rules of a procurement regime that can be applied once a Member State has invoked Art.296 EC.³⁶ It does not, however, give guidelines as to the circumstances when the exemption itself could be used, despite the fact that some have argued that this might be the most important issue of the defence procurement debate.³⁷

The Code of Conduct may be applied to all defence procurement opportunities of €1 million or more where the conditions for application of Art.296 EC are met, except for:

- Procurement of research and technology;
- Collaborative procurement;
- Procurement of nuclear weapons and nuclear propulsion systems;

³² EDA Steering Board Decision No. 2005/03/EDA of 5 June 2005 on European Defence Equipment Market

³³ European Defence Agency Press Release, 'EU Governments Agree Voluntary Code for Cross-Border Competition in Defence Equipment Market', Brussels, 21 November 2005; European Defence Agency Press Release, 'EDA Welcomes European Commission Move on Defence Procurement Rules', Brussels, 6 December 2005

³⁴ European Defence Agency Press Release, 'EDA Steering Board Takes further Step towards Injecting Competition into Defence Procurement', Brussels, 23 September 2005

³⁵ EDA Steering Board Decision on an Intergovernmental Regime to Encourage Competition in the European Defence Equipment Market, Brussels, November 21, 2005; European Defence Agency Press Release, 'EU Governments Agree Voluntary Code for Cross-Border Competition in Defence Equipment Market', Brussels, 21 November 2005

³⁶ The Code of Conduct on Defence Procurement of the EU Member States Participating in the European Defence Agency, Brussels, 21 November 2005, found at <http://www.eda.eu.int/reference/eda/EDA%20-%20Code%20of%20Conduct%20-%20European%20Defence%20Equipment%20Market.htm> accessed on 25 November 2005

³⁷ Georgopoulos A., 'The European Defence Agency's Code of Conduct for Armament Acquisitions: A Case of Paramnesia?', (2006) 15(2) PPLR 55, p.57

- Procurement of chemical, bacteriological and radiological goods and services; and
- Procurement of cryptographic equipment.

Under the Code of Conduct, even though this is not explicitly stated, defence procurement should generally be performed through competitive procurement procedures. However, subscribing Member States may exceptionally perform specific procurements without competition:

- In cases of pressing operational urgency;
- For follow-on work or supplementary goods and services; or
- For extraordinary and compelling reasons of national security.

The first characteristic of the Code of Conduct is that it is *voluntary and non-binding*. The EDA participating Member States are free to subscribe to the regime, thereby becoming ‘subscribing Member States’ (sMS).³⁸ Moreover, no legal penalty is attached for the actual non-observance of the Code of Conduct by a subscribing Member States, but the regime applies between subscribing Member States on a reciprocal basis.

Second, the regime promotes the *fair and equal treatment of suppliers* from other subscribing Member States. Equal treatment is to be ensured through transparency and equality of information, transparent and objective selection criteria, technical specifications expressed in functional terms and based on international standards, clear award criteria that should lead to the selection of the most economically advantageous tender, and the debriefing of unsuccessful bidders. Contract award may take into account inter alia considerations of costs (both acquisition and life cycle), compliance, quality, security of supply and offsets.

Third, the regime is based on *mutual transparency and accountability*. The EDA will collect data on the operation of the regime (including on instances when no competition was performed and on collaborative procurement) and, on that basis, subscribing Member States will have the opportunity to question each other and justify themselves for invoking the

³⁸ All participating Member States subscribed to the regime from the start, except Spain and Hungary who joined in July 2007, and Bulgaria and Romania that are considering joining following their entry into the EU and becoming EDA participating Member States: European Defence Agency Press Release, ‘Spain to Join Code of Conduct for European Defence Equipment Market’, Brussels, 19 June 2007; see also Murphy J. and Fiorenza N., ‘Hungary, Spain Reject EDA Code’, Jane’s Defense Weekly, 31 May 2006, p.20

Art.296 EC exemption and for deviating from the Code of Conduct ('institutionalised peer pressure' or 'moral coercion'³⁹).

Fourth, the Code of Conduct promotes *mutual support* between subscribing Member States to ensure security of supply and the predictability and dependability of their regulations and policies. These provisions are complemented by an EDA initiative related to security of supply, which is discussed below.

Fifth and lastly, the Code of Conduct plans to achieve *mutual benefit* for all subscribing Member States, especially through the involvement of Small and Medium Enterprises (SME) through a complementary Code of Best Practice in the Supply Chain (described in the section below).

The Code of Conduct is actually very similar to the defunct Coherent Policy Document of the Western European Armaments Group (WEAG) that was already supposed to create a European defence equipment market.⁴⁰ The fact that it is non-binding is considered by some as its main weakness.⁴¹ However, its context is significantly dissimilar in terms of institutional structure, timing and the use of peer pressure and reciprocity, and it probably has better prospects of achieving concrete results,⁴² even though some consider that the goal of the Code of Conduct to help creating a common market for defence equipment remains a long-term hope rather than a foreseeable reality.⁴³

The Code of Conduct does not define rules in any details and is limited to broad principles that leave a number of questions unanswered, as well as room for varying implementation among the subscribing Member States. This means that the actual procurement procedures applied by the subscribing Member States when the Art.296 EC exemption is invoked will remain national, and will not be subject to a harmonisation process (as would be the case if an EC directive was adopted). This is one of the drawbacks of the Code of Conduct, as the

³⁹ Kuechle H., 'The cost of non-Europe in the area of security and defence', above fn.2, §4.3

⁴⁰ Georgopoulos A., 'The European Defence Agency's Code of Conduct for Armament Acquisitions: A Case of Paramnesia?', above fn.37, pp.61-62; Schmitt B. (rapporteur), 'Defence Procurement in the European Union – The Current Debate', above fn.1, pp.39

⁴¹ Kuechle H., 'The cost of non-Europe in the area of security and defence', above fn.2, p.47

⁴² Georgopoulos A., 'The European Defence Agency's Code of Conduct for Armament Acquisitions: A Case of Paramnesia?', above fn.37, pp.63-64

⁴³ Neuman S., 'Defense Industries and Dependency: Current and Future Trends in the Global Defense Sector', International Relations and Security Network (ISN), 2006, p.18

defence industry will still have to cope with differing procurement procedures between the EU Member States for 'hard' defence material.⁴⁴

We saw above that the Code of Conduct allows the subscribing Member States to conduct their procurement activities without competition for 'extraordinary and compelling reasons of national security'. This provision allows the subscribing Member State that invokes it to avoid the application of most of the provisions of the Code of Conduct (especially those on equal treatment), even though some other provisions such as mutual support, accountability and mutual benefit (including the Code of Best Practice in the Supply Chain) should still apply. It has been argued that the strong wording 'extraordinary and compelling' is meant to underline that the exemption should be applied only in the most exceptional of cases.⁴⁵ This is logical, as the Code of Conduct is already supposed to apply only when the Art.296 EC exemption applies, and a further exemption from the Code of Conduct should therefore have an even narrower scope. However, this exemption could still be abused by subscribing Member States, even though 'peer pressure' could limit such abuse. Only time will tell if this peer pressure will prove sufficiently effective.

In addition, there seems to be some inherent contradiction in the reasoning behind the Code of Conduct idea. It is arguably quite difficult to, on the one hand, claim for an exemption (e.g. Art.296 EC) from compliance with the EC Treaty and any public procurement directive because the essential security interests of a Member State are involved, while on the other hand publishing the related procurement opportunity and complying with generic principles of competition and equal treatment, which seem to be very similar to those that the ECJ found in the EC Treaty.⁴⁶

⁴⁴ Kuechle H., 'The cost of non-Europe in the area of security and defence', above fn.2, p.46

⁴⁵ Georgopoulos A., 'The European Defence Agency's Code of Conduct for Armament Acquisitions: A Case of Paramnesia?', above fn.37, p.59

⁴⁶ Such as: non-discrimination on the grounds of nationality: Case C-3/88, *Commission v Italy* [1989] ECR 4035 (*data processing*), Case 21/88, *Du Pont de Nemours Italiana S.p.A. v Unità Sanitaria Locale No. 2 di Carrara* [1990] ECR I-889, Case C-113/89, *Rush Portuguesa Lda v Office national d'immigration* [1990] ECR I-1417, Case C-243/89, *Commission v Denmark* [1993] ECR I-3353 (*Storebaelt Bridge*); transparency: Case 45/87, *Commission v Ireland* [1988] ECR 4929 (*Dundalk water pipes*), at [16]; Case C-275/98, *Unitron Scandinavia A/S and 3-S A/S, Danske Svineproducenters Serviceselskab v Ministeriet for Fødevarer, Landbrug og Fiskeri* [1999] ECR I-8291, at [31]; Case C-324/98, *Telaustria and Telefonadress v Telekom Austria* [2000] ECR I-10745, Case C-231/03, *Consorzio Aziende Metano (Coname) v Comune di Cingia de' Botti*, judgement of 21 July 2005; or equal treatment of tenderers: Case C-3/88, *Data Processing*, above; Case C-458/03, *Parking Brixen GmbH v Gemeinde Brixen and Stadtwerke Brixen AG*, judgement of 13 October 2005; Case C-410/04, *Associazione Nazionale Autotrasporto Viaggiatori (ANAV) v Comune di Bari and AMTAB Servizio SpA*, judgement of 6 April 2006

4.2. Code of Best Practices in the Supply Chain

However, the Code of Conduct was not considered sufficient to reduce the fragmentation of the European defence equipment market. Therefore, at the time of the approval of the Code of Conduct, the participating Member States tasked the EDA to develop a Code of Best Practice in the supply chain, to ensure fair opportunities of subcontracting, especially for SME.⁴⁷ A proposal of the Agency was reviewed and approved by the Aerospace and Defence industries Association (ASD), and finally approved by the EDA Steering Board on 15 May 2006.⁴⁸

The Code of Best Practice⁴⁹ is an integral part of the Code of Conduct, is voluntary, is complementary to national procedures, and applies when the Code of Conduct does. It aims at increasing transparency and fair competition at the contract and sub-contract level. Under the Code of Best Practice, the prime contractor remains responsible for its supply chain, subject to legal or other requirements of the subscribing Member States. The Code of Best Practice promotes opportunities for qualified and competent suppliers, including SME, to participate in competitions on a level playing-field basis, when competition is efficient, practical and economically or technologically appropriate. It includes, for the selection of subcontractors, principles similar to those of the Code of Conduct, such as selection of the most economically advantageous bid, the use of best practices, and the monitoring of subcontracting opportunities through advertising.

The Code of Best Practice seems to be a good general basis to flow down the supply chain the potential benefits to be gained from the Code of Conduct. However, it remains again very general, and its effectiveness will depend on the willingness of the subscribing Member States to enforce it and of the prime contractors to actually apply it. Even though its approval by the Aerospace and Defence industries Association is to be seen as a step in the right direction to involve the European defence industry in the regulation of defence procurement, the resulting

⁴⁷ EDA Steering Board Decision on an Intergovernmental Regime to Encourage Competition in the European Defence Equipment Market, Brussels, November 21, 2005

⁴⁸ EDA Steering Board Decision Approving the Code of Best Practice in the Supply Chain, Brussels, May 15, 2006

⁴⁹ The Code of Best Practice in the Supply Chain Approved by Aerospace and Defence industries Association on 27 April and agreed by the EU Member States Participating In The European Defence Agency, Brussels, 15 May 2006, found at <http://www.eda.europa.eu/reference/eda/E.D.A.%20-%20Code%20of%20Best%20Practice%20in%20the%20Supply%20Chain%20-%20European%20Defence%20Equipment%20Market.htm>, accessed on 26 May 2006

document still leaves a wide scope of flexibility to all parties involved.⁵⁰ For instance, its deference to ‘legal or other requirements of the subscribing Member States’, accommodates security of supply, but also allows the healthy survival of offsets and other market distortions, especially since offsets are amongst the allowed award criteria under the Code of Conduct. One of the missing pieces of the EDA intergovernmental regime seems therefore to be the harmonisation of offsets practices.

One of the reasons why contracting authorities in the field of defence refrain from dealing directly with SME is the concern that SME cannot ensure product support over the whole life of military equipment (often 20-50 years⁵¹), thereby not being able to ensure security of supply over the long term. It seems that the Code of Best Practice attempts to shift this risk towards prime contractors, which might be a good strategy (even though technologically risky), but only if the major European defence industries are willing to play their part, which hopefully can be presumed from the fact that the Aerospace and Defence industries Association approved the Code of Best Practice.

4.3. Electronic Bulletin Board

At the time of the approval of the Code of Conduct, the participating Member States tasked the EDA to develop a single portal for announcement of all new contracting opportunities.⁵² This Electronic Bulletin Board (EBB) became operational on time⁵³ and constitutes one of the specificities of the EDA intergovernmental regime. Its physical aspect is quite similar to the Tenders Electronic Daily (TED) database used for the publication of notices under the EC Public Sector Directive.⁵⁴ In the year following the entry into force of the regime, governments have advertised nearly 200 contract opportunities worth approximately 10

⁵⁰ For additional comments, see Georgopoulos A., ‘European Defence Agency: The New Code of Best Practice in the Supply Chain’, (2006) 15(5) PPLR NA145

⁵¹ COM(2004) 608, above fn.1, §2.3

⁵² EDA Steering Board Decision on an Intergovernmental Regime to Encourage Competition in the European Defence Equipment Market, Brussels, November 21, 2005

⁵³ European Defence Agency Press Release, ‘Steering Board Agrees Key Measures for Launch of Defence Procurement Code of Conduct in July’, Brussels, 7 April 2006

⁵⁴ See the TED database at <http://ted.europa.eu>, accessed on 24 September 2007

billion € on the Electronic Bulletin Board.⁵⁵ Those opportunities cover not only major equipment procurement, but also many maintenance requirements.⁵⁶

Considering that the figures presented above showed that about 85.7 billion € were spent by the participating Member States in 2005 for major equipment procurement, R&D, operations and maintenance, the initial success of the Electronic Bulletin Board over its first year seems to be reasonably significant, especially in contrast with the publication rate of contracting authorities in the field of defence in the EC TED database (for procurement covered by the EC public procurement directives), which is about 10%, while the average is about 25% for all other contracting authorities.⁵⁷

As of 24 September 2007, a total of 250 notices had been published on the Electronic Bulletin Board (184 for goods and 66 for services). Of these notices, 54 were Prior Information Notices (PIN), 16 were open Contract Notices (CN), 141 were expired Contract Notices, and 34 were Contract Award Notices (CAN).⁵⁸ The total value of the awarded contracts was estimated at more than 156 million € with about 55% of such contracts awarded to SME, but only about 15% awarded to a bidder from another country (of which less than half were from an EU country).⁵⁹ This could be considered a disappointing result for cross-border competition, even though it is difficult to tell if this is because there were few tenderers from other EU countries, or if this shows a national preference at the time of contract award.

Moreover, the rate of publication in the Electronic Bulletin Board varies widely between subscribing Member States, and not necessarily because of size. The number of notices published by each subscribing Member State is shown on Table 1.

⁵⁵ European Defence Agency Press Release, 'Spain to Join Code of Conduct for European Defence Equipment Market', Brussels, 19 June 2007 Summary of Report to EDA Steering Board on Working of Defence Procurement Code of Conduct Brussels, 25 September 2007, <http://www.eda.europa.eu/newsitem.aspx?id=253>, accessed on 3 October 2007

⁵⁶ See the list of notices at <http://www.eda.europa.eu/ebbweb>

⁵⁷ COM(2005)626, above fn.18, p.4

⁵⁸ Source: EBB website at <http://www.eda.europa.eu/ebbweb/bycountry.aspx>, accessed on 24 September 2007 – The number of different types of notices does not add-up to 250, which is evidence of a probable minor bug in the EBB

⁵⁹ Summary of Report to EDA Steering Board on Working of Defence Procurement Code of Conduct Brussels, 25 September 2007, <http://www.eda.europa.eu/newsitem.aspx?id=253>, accessed on 3 October 2007; Of the 34 awarded contracts, 2 were awarded to a contractor from another EU country (by Sweden to a UK contractor and by Belgium to a Spanish contractor), and 3 to contractors from non-EU countries (by UK to two contractors from Brazil and Switzerland, by the Netherlands to a US contractor, and by Slovenia to a Swiss contractor)

| <i>Member State</i> | <i>Published Notices</i> | <i>Percentage of Total</i> |
|---|--------------------------|----------------------------|
| France | 60 | 24.0% |
| Poland | 45 | 18.0% |
| Netherlands | 36 | 14.4% |
| Sweden | 23 | 9.2% |
| Germany | 22 | 8.8% |
| Finland | 18 | 7.2% |
| United Kingdom | 15 | 6.0% |
| Slovenia | 8 | 3.2% |
| Italy | 7 | 2.8% |
| Cyprus | 6 | 2.4% |
| Czech Republic | 3 | 1.2% |
| Portugal, Lithuania, Slovakia | 2 each | 0.8% each |
| Belgium | 1 | 0.4% |
| Austria, Estonia, Greece, Hungary, Ireland, Latvia, Luxemburg, Malta, Spain | None | 0.0% each |
| <i>Total</i> | 250 | - |

Table 1: Notices Published in the EBB per Subscribing Member State from 1 July 2006 to 24 September 2007⁶⁰

A few comments must be made on these results. As Spain and Hungary only became subscribing Member States three months before the data was collected, it is not surprising that they had no published notices. Likewise, the size of the armed forces of Estonia, Latvia, Luxemburg, Malta and Slovenia is very small (smaller than 7000 people each),⁶¹ and the relatively high quantity of notices published by the latter is probably more surprising than the fact that the others published none.

⁶⁰ Source: EBB website at <http://www.eda.europa.eu/ebbweb/bycountry.aspx>, accessed on 24 September 2007

⁶¹ European Defence Agency, 'National Breakdowns of European Defence Expenditure', February 2007, p.7

Figure 2 shows, in percentage for each subscribing Member State, its armed forces personnel relative to the total number of armed forces personnel in the EU in 2005, its defence expenditures for 2005 relative to the total EU defence expenditures, and the number of Electronic Bulletin Board notices it published up to 24 September 2007 relative to the total number of published notices. This graph shows clearly some inconsistencies in the number of published notices and the size of the Member States concerned from a defence point of view. Among the ‘larger’ Member States, if the publication rates for France, Poland, the Netherlands or Sweden are any indication, then the publication rates of Germany, Italy and the UK seem low.⁶² This could be either a sign that they invoke the Art.296 EC exemption only rarely, or that they somehow spurn the systematic application of the Code of Conduct. It remains to be seen if peer pressure will be effectively applied.

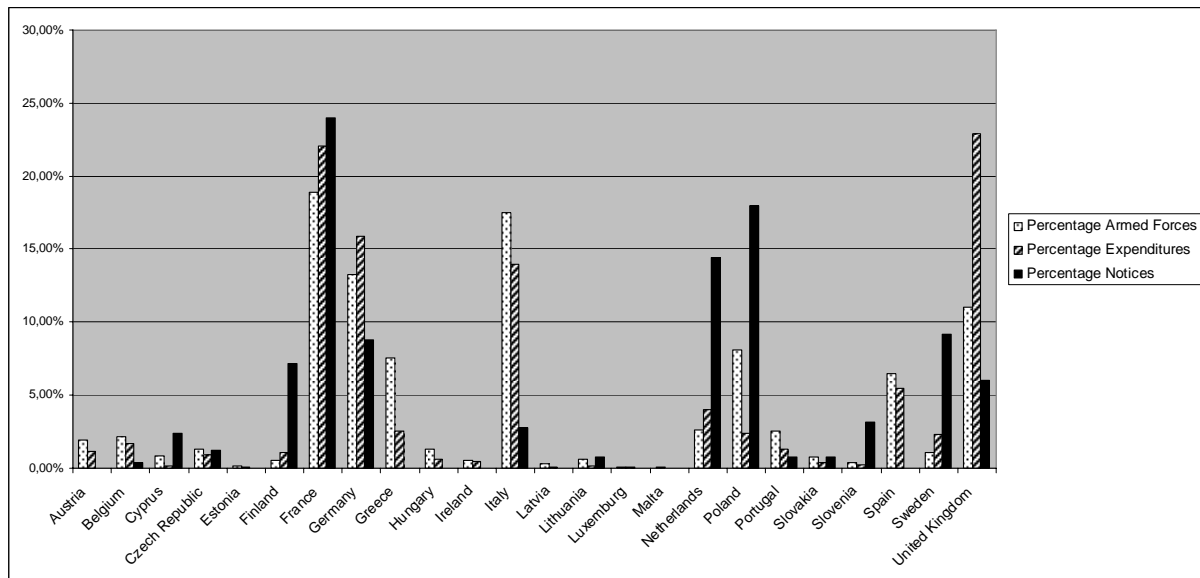


Figure 2: Armed Forces Size, Defence Expenditures, and Number of EBB Notices⁶³

It is also worth noting that Poland was by far the subscribing Member States who published the most CAN (16 out of 34), but that each contract was awarded to a Polish company.⁶⁴

⁶² Greece has an important conscript army and performs a lot of activities in-house, which means that its equipment procurement budget (and therefore the expected number of notices) is actually limited – even though no notices at all seems surprising: see Mawdsley J., Quille G. et.al., ‘Equipping the Rapid Reaction Force – Options for and Constraints on a European Defence Equipment Strategy’, above fn.21, p.24

⁶³ European Defence Agency, ‘National Breakdowns of European Defence Expenditure’, February 2007 and EBB website at <http://www.eda.europa.eu/ebbweb/bycountry.aspx>, accessed on 24 September 2007

⁶⁴ Source: EBB website at <http://www.eda.europa.eu/ebbweb/bycountry.aspx>, accessed on 24 September 2007

As of 1 September 2007, the EDA had been informed of 83 government contracts falling under the exceptions of the Code of Conduct, mostly for ‘supplementary goods and services’ and ‘follow-on work’. This was qualified as ‘a reasonable and relatively restrictive use of the follow-on exceptions’.⁶⁵ However, this represents nevertheless more than 36% of the number of notices published at that time.

The Electronic Bulletin Board also includes ‘vademecums’ on the defence procurement legislation and practices of the individual participating Member States. As of 24 September 2007, this included reasonably detailed information for 19 participating Member States.⁶⁶ This consists often of links to national information portals on defence procurement.

In line with the principles set-out in the Code of Best Practice, since March 2007, the Electronic Bulletin Board has also displayed industry-to-industry sub-contracting opportunities for defence equipment. During the first three months of operation of that feature, more than 100 such opportunities have been advertised.⁶⁷ As of 24 September 2007, a total of 28 different branches of companies belonging to 18 major companies or groups had published a total of 135 notices (82 for goods, 11 for services, 41 for both goods and services, and 1 for development). Of these notices, 115 were the equivalents to Prior Information Notices (SPIN), 5 were open equivalents to Contract Notices (SCN), 15 were expired equivalents to Contract Notices (SCN), and there had been no equivalent to Contract Award Notices (SCAN).⁶⁸ The skewed repartition between types of notices is probably simply an indication that only seven months elapsed between the start of the system and the collection of the data. The published industry-to-industry notices as of 1 September 2007 amounted to about 120 million €⁶⁹

This also seems to be a promising start, perhaps even more encouraging than the publication rate of subscribing Member States, and probably shows that the defence industry is more

⁶⁵ Summary of Report to EDA Steering Board on Working of Defence Procurement Code of Conduct Brussels, 25 September 2007, <http://www.eda.europa.eu/newsitem.aspx?id=253>, accessed on 3 October 2007

⁶⁶ See <http://www.eda.europa.eu/ebbweb/vademecum.aspx>, accessed on 24 September 2007 (Cyprus, Hungary, Luxemburg, the Netherlands and Spain were not included, which for Hungary and Spain can be explained by the fact that they joined the intergovernmental regime three months before)

⁶⁷ European Defence Agency Press Release, ‘Spain to Join Code of Conduct for European Defence Equipment Market’, Brussels, 19 June 2007

⁶⁸ source: EBB website at <http://www.eda.europa.eu/ebbweb/bycompany.aspx>, accessed on 24 September 2008

⁶⁹ Summary of Report to EDA Steering Board on Working of Defence Procurement Code of Conduct Brussels, 25 September 2007, <http://www.eda.europa.eu/newsitem.aspx?id=253>, accessed on 3 October 2007

systematically putting cost-effectiveness before national preference than the subscribing Member States, which should not come as a surprise. However, the EDA considered that more needed to be done to raise the awareness of industry.⁷⁰

4.4. Framework Arrangement for Security of Supply

At the time of the approval of the Code of Conduct, the participating Member States tasked the EDA to work further with them on security of supply and the harmonisation of offset requirements.⁷¹ Security of supply is one of the key characteristics of the defence market, and aims to ensure on the one hand the stability and continuity of the supply chain over the life of military equipment, which can be up to 50 years ('longer-term' security of supply), and on the other hand the ability of the supply chain to cope with 'surges' in requirements during operations ('short-term' security of supply). To be efficient, security of supply must be ensured despite shifts in alliances, and must take into account possible disturbances of the supply chain due to international unrest. The easiest way, but most disrupting of market efficiency, to accommodate security of supply has often been to award defence contracts only to national companies or to require military offsets to build or consolidate a defence equipment capability on national soil.⁷² Short-sighted enforcement of security of supply is one of the most likely causes of the current European defence equipment market fragmentation.⁷³

However, the geopolitical situation of Europe changed dramatically since the end of the Cold War and with the increasing integration within the EU, and the concept of security of supply within Europe clearly requires re-evaluation.⁷⁴ To accommodate security of supply within a changed Europe and a more and more integrated defence industry, it was first of all considered especially important to define priority rules for access to defence equipment in

⁷⁰ Summary of Report to EDA Steering Board on Working of Defence Procurement Code of Conduct Brussels, 25 September 2007, <http://www.eda.europa.eu/newsitem.aspx?id=253>, accessed on 3 October 2007

⁷¹ EDA Steering Board Decision on an Intergovernmental Regime to Encourage Competition in the European Defence Equipment Market, Brussels, November 21, 2005

⁷² Vlachos K., 'Safeguarding European Competitiveness – Strategies for the Future European Arms Production and Procurement', Occasional Paper No 4, Institute for Security Studies, WEU, January 1998, Chapter 2.1; COM(2004) 608, above fn.1, §2.2

⁷³ See further the discussion in Schmitt B., 'From Cooperation to Integration: Defence and Aerospace Industries in Europe', above fn.20, pp.60-62; COM(2003) 113, above fn.20, p.18; Mezzadri S., 'L'ouverture des Marchés de la Défense: Enjeux et Modalités', above fn.12, p.6

⁷⁴ COM(2003) 113, above fn.20, p.18

case of emergency.⁷⁵ The EDA Steering Board therefore approved a framework arrangement on security of supply in circumstances of operational urgency on 20 September 2006.⁷⁶

Under that arrangement, subscribing Member States agreed that they will do everything possible, consistent with national law and international obligations to assist and expedite each others' contracted defence requirements, particularly in circumstances of pressing operational urgency, and to work to increase the level of mutual confidence amongst themselves, in particular by improving the predictability of their policies. If, in times of emergency, crisis or armed conflict, a subscribing Member State requests defence goods or services from other subscribing Member States, they will engage in immediate consultation with the requesting subscribing Member State, with the aim of ensuring that the need is met as expeditiously as possible. In addition to taking all possible steps to expedite its administrative processes, each subscribing Member States will also, if so requested by another subscribing Member State, engage with suppliers on its territory to help ensure that an appropriate priority is given to the needs of the requesting subscribing Member States (the requesting subscribing Member States will meet any additional cost), and will consider 'urgently and sympathetically' any request for provision of defence goods from its own stocks, mainly on a re-imbusement basis.

These provisions are again general, and are based on the principles of consultation and mutual support inherent to the Code of Conduct. As such, they can only be successful if the subscribing Member States apply them in good faith. Even though they clearly constitute a step in the right direction to ensuring security of supply, it remains to be seen how they will be implemented. For instance, it is unclear how this commitment would be applied, if at all, in situations where some subscribing Member States participate in an operation that other subscribing Member States oppose (e.g. the second Iraq war).

Moreover, these provisions only concern what we called the 'short-term' security of supply, in case of urgent operational need. This is relatively uncontroversial, as any subscribing Member States usually would recognise in principle that they should provide support to other subscribing Member States in these cases. In addition to what we mentioned above, a key issue with that type of security of supply is one of practical priorities: many, if not all,

⁷⁵ Tigner B., 'EDA Ponders Defense Supply Procedure', Defence News, 31 July 2006

⁷⁶ EDA Steering Board Decision on a Framework Arrangement for Security of Supply between Subscribing Member States (sMS) in Circumstance of Operational Urgency, 20 September 2006, <http://www.eda.europa.eu/reference/sbd/sbd-2006-09-0.htm>

subscribing Member States are likely sometimes to be involved in urgent operations at the same time (e.g. the ongoing war in Afghanistan), and therefore to impose conflicting demands on the defence industry. No generic arrangement can resolve satisfactorily the allocation of scarce resources to multiple customers.

The framework arrangement does not really address 'longer-term' security of supply, such as how to avoid continuous hindrances or interruption of the supply chain through a subscribing Member States' administrative measures for political or economical reasons. A subscribing Member States could also entice national companies to shift their priorities away from supporting systems bought by another subscribing Member States and towards national-oriented programmes. Longer-term security of supply should also address how the viability of companies, especially SME, located in other subscribing Member States would be ensured. Only when these issues are also satisfactorily covered can full security of supply be ensured. The EDA seems to recognise this shortfall and that more needs to be done on security of supply.⁷⁷

In addition, the Code of Best Practice, with its emphasis on ensuring the participation of SME in the defence market, can be seen as somewhat contradicting security of supply as, as we mentioned above, there is a concern that SME cannot ensure product support over the long life of military equipment. Even though the Code of Best Practice attempts to shift this risk towards the prime contractors, it remains to be seen if this will be successful in ensuring security of supply.

Moreover, the EDA proposals on the harmonisation of offset requirements are still in preparation. A study was recently provided to the EDA on the subject, for further discussion with the participating Member States.⁷⁸ This study performed a mapping of European offsets, analysed the legal context of offsets, and analysed the effect of offsets on the European defence equipment market and its future development, but highlighted that little information was available on the issue. Even though this is a very complex issue,⁷⁹ harmonisation of offset

⁷⁷ Summary of Report to EDA Steering Board on Working of Defence Procurement Code of Conduct Brussels, 25 September 2007, <http://www.eda.europa.eu/newsitem.aspx?id=253>, accessed on 3 October 2007

⁷⁸ Eriksson E.A. et.al., 'Study on the effects of offsets on the Development of a European Defence Industry and Market', Final Report of 06-DIM-022, FOI and SCS, 12 July 2007

⁷⁹ As explained in details in Georgopoulos A., *European Defence Procurement Integration*, above fn.9

practices has to be tackled if the EDA intergovernmental regime is to be fully effective, especially since the Code of Conduct allow the use of offsets as contract award criteria.

4.5. Security of Information

It was soon recognised that, in order to promote cross-border competition through the EDA intergovernmental regime, additional action was required to protect classified information released to industry in other subscribing Member States, to ensure that there would be no discrimination against company from other subscribing Member States on the grounds of security of information, and as well to protect commercially sensitive information provided by companies to the subscribing Member States.⁸⁰

The EDA Steering Board therefore decided that subscribing Member States would use the EU Council security regulations,⁸¹ and agreed common minimum standards on industrial security⁸² for their procurement under the Code of Conduct that require protection of classified information. The latter is to apply when the use of bilateral security agreements is not possible or not appropriate.

The Council security regulations lay down the basic principles and minimum standards of security to be respected by the EU institutions and Member States so that security is safeguarded and that each may be assured that a common standard of protection is established.⁸³ To that end, they cover the organisation of security, the management of the security classification of information, physical security (e.g. access control measures), rules on need to know and security clearance of officials, release of information to third parties, and how to deal with breaches of security. Such procedures are standard practice in any organisation dealing with defence and security matters.

Moreover, subscribing Member States committed not to disclose information forwarded to them within the framework of the Code of Conduct by companies that have designated that information as confidential, subject to national law and to the transparency provisions of the

⁸⁰ Tigner B., 'EDA Ponders Defense Supply Procedure', above fn.75

⁸¹ Council Decision 2001/264/EC of 19 March 2001 adopting the Council's security regulations, OJ 2001 L 101/1, as amended by Council Decisions 2004/194/EC of 10 February 2004, 2005/571/EC of 12 July 2005 and 2005/952/EC of 20 December 2005

⁸² Security of Information Between Subscribing Member States (sMS) – Common Minimum Standards on Industrial Security, 20 September 2006, <http://www.eda.europa.eu/reference/sbd/SoI.pdf>

⁸³ Council Decision 2001/264/EC, supra fn.31, Annex, Part I, 1

Code of Conduct.⁸⁴ The latter probably means that information about the particular procurement would still have to be shared with the EDA and the other subscribing Member States.

These decisions are a welcome complement to the Code of Conduct, and have the potential to remove one additional ground for discriminating against companies from other subscribing Member States. As such, they can only have a positive effect.

5. Coherence with European Commission Initiatives

In order to better define possible actions to liberalise defence procurement, the Commission of the EC initiated in 2004 a consultation on the subject, where it proposed two possible actions: publishing an interpretative communication on the existing legal framework, and initiating a new legal instrument specifically applicable to ‘hard’ defence procurement.⁸⁵ It seems clear that the Commission intended to limit as much as possible the impact of Art.296 EC, but recognised the difficulties inherent to the specificities of the defence market.⁸⁶

Commentators welcomed this consultation.⁸⁷ The EDA stood by the proposals of the Commission, adding that it was ready to support this process, and mentioned its ongoing work on its voluntary regime for the application of Art.296 EC.⁸⁸ Others submitted that the use of Art.296 EC should be made clearer and more transparent, but that an interpretative communication, although useful, would not be sufficient, and that defence procurement law should be harmonised, preferably by the use of a new directive.⁸⁹

⁸⁴ EDA Steering Board Decision on Security of Information Between Subscribing Member States (sMS), Brussels, 20 September 2006, <http://www.eda.europa.eu/reference/sbd/sbd-2006-09-1.htm>

⁸⁵ COM(2004) 608, above fn.1; see also Mingasson J-P., speech at the ‘Réunion POLARM – Séminaire informel sur l’Industrie de la Défense’, Brussels, 5 November 2003; Bacri P-P., ‘Les Institutions Européennes et l’Armement’, 75 CAIA Bulletin 14, 2004; see also Schmitt B. (rapporteur), ‘Defence Procurement in the European Union – The Current Debate’, above fn.1, pp.17 et.seq.

⁸⁶ ‘Public procurement: Commission consults on more open and efficient defence procurement’, IP/04/1133, 23 September 2004; ‘Public Procurement: Commission consults on more open and efficient defence procurement – Frequently Asked Questions’, MEMO/04/222, 23 September 2004

⁸⁷ Georgopoulos A., ‘The Commission’s Green Paper on Defence Procurement’, (2005) 14(2) PPLR NA34

⁸⁸ Decision No 2005/02/EDA of 2 March 2005 of the EDA Steering Board in NADs formation on EDA input to the Commission’s consultation process on the Green Paper

⁸⁹ See e.g. EU Institute for Security Studies, ‘Contribution to the Consultation “Green Paper on Defence Procurement” – Answers and Comments made by the EUISS Task Force on the establishment of a European Defence Equipment Market’, 15 February 2005; Georgopoulos A., ‘Green Paper on Defence Procurement – Contribution to the Consultation process for the establishment of a European Defence Equipment Market’,

On that basis, the Commission published a new communication summarising the results of the consultation and outlining its action plan.⁹⁰ The latter included the publication of an interpretative communication on the application of Art.296 to defence procurement in 2006 and, as the EC Public Sector Directive was considered unsuitable for ‘hard’ defence procurement activities, the issue in 2007 of a proposal for a directive for the procurement of arms, munitions and war material and related services that would take into account the specific needs of ‘hard’ defence procurement and would apply when the Art.296 EC exemption is not invoked. This approach has been qualified as providing a ‘stick’ and a ‘carrot’, as the interpretative communication would threaten the Member States with the ‘stick’ the Commission would use if invoking Art.296 EC was, in its view, unwarranted, while the Defence Procurement Directive would provide a ‘carrot’ allowing the Member States to use more flexible procedures should they not invoke the exemption.⁹¹

The Commission’s action plan has to be seen in the context of the most recent developments of EC public procurement law. The ECJ has now ruled that transparency, sufficient advertising,⁹² and not only non-discrimination, but also equal treatment of suppliers and some form of competition,⁹³ were obligations on contracting authorities that flowed from the EC Treaty and applied even if the EC public procurement directives would not apply. In addition, it is most likely that the Public Sector Directive applies to all defence procurement as long as Art.296 EC or another applicable exemption is not invoked.⁹⁴ This context is an incentive for

Dundee, 2005; The results of the consultation can be found at http://www.europa.eu.int/comm/internal_market/publicprocurement/dpp_en.htm

⁹⁰ COM(2005)626, above fn.18; Public procurement: new Commission initiatives on more open and efficient defence procurement, IP/05/1534, Brussels, 6 December 2005; see also the slightly different analysis in Michel J. and Rivière J., rapporteurs, ‘Rapport d’Information sur les nouveaux défis de la construction de l’Europe de la défense’, Commission de la Défense Nationale et des Forces Armées, French National Assembly, N° 2531, 27 September 2005, pp.42 et.seq., highlighting that France and the United Kingdom did not support an interpretative communication or a directive, and that other Member States were at best lukewarm

⁹¹ Georgopoulos A., ‘Commission’s Communication on the Results of the Consultation Process on European Defence Procurement’, (2006) 15(4) PPLR NA119; see also Schmitt B., ‘The European Union and Armaments – Getting a Bigger Bang for the Euro’, above fn.28, pp.55 et.seq., who clearly anticipated the Commission’s action plan

⁹² Case 45/87 *Dundalk water pipes*, above fn.46, at [16]; Case C-275/98 *Unitron Scandinavia*, above fn.46, at [31]; Case C-324/98 *Telaustria*, above fn.46, at [60]-[62]; Case C-231/03 *Coname*, above fn.46, at [16]

⁹³ Case C-3/88 *Data Processing*, above fn.46, at [8]; Case C-458/03 *Parking Brixen*, above fn.46, at [46]-[49]; Case C-410/04 *ANAV*, above fn.46, at [18]-[24]

⁹⁴ See the wording of Directive 2004/18/EC, above fn.5, Art.10 and the discussion in Trybus M., ‘Defence Procurement: The New Public Sector Directive and Beyond’, above fn.1, §2; Heuninckx B., ‘Defence Procurement in the EU: Time to Listen to the Wake-up Calls’, above fn.1; COM(2004) 608, above fn.1, §3.1

the EC Member States to agree an instrument under the EC Treaty that would better fit to 'hard' defence procurement than the Public Sector Directive before the ECJ finally adopts a restrictive approach of the Art.296 EC exemption and forces the Member States to comply with the Public Sector Directive for most of their defence procurement.⁹⁵

The EDA welcomed the Commission proposals, qualifying them as complementary to the Code of Conduct.⁹⁶ It has been argued that the harmonisation of the national defence procurement rules by a Defence Procurement Directive would be especially beneficial.⁹⁷ A Defence Procurement Directive could also resolve the inherent contradiction of the Code of Conduct mentioned above (Member States invoking an exemption from the EC Treaty but nonetheless willing to publish and compete their procurement), by enticing the Member States to remain within the scope of the EC Treaty.

The interpretative communication on the application of Art.296 EC to defence procurement was published in late 2006.⁹⁸ It defines the view of the Commission on the conditions under which the Art.296 EC exemption may be used.⁹⁹ It has been argued that the apparent willingness of the Commission to institute proceedings against Member States who overuse the Art.296 EC exemption may promote compliance with the Code of Conduct.¹⁰⁰

However, when the Code of Conduct was approved, the coherence of the EDA approach with the ongoing initiatives of the Commission has been rightly questioned. In particular, the Commission's view on the review of the use of the Art.296 EC exemption (based on objective grounds) is fundamentally at odds with the monitoring and peer pressure process established by the Member States through the Code of Conduct to review their subjective decisions to

⁹⁵ A similar argument is made in a broader context in Arrowsmith S., 'The Past and Future Evolution of EC Procurement Law: From Framework to Common Code?', (2006) 35 PCLJ 337

⁹⁶ European Defence Agency Press Release, 'EDA Welcomes European Commission Move on Defence Procurement Rules', Brussels, 6 December 2005

⁹⁷ Schmitt B. (rapporteur), 'Defence Procurement in the European Union – The Current Debate', above fn.1, pp.15-16

⁹⁸ Interpretative Communication on the application of Article 296 of the Treaty in the field of defence procurement (presented by the Commission), COM(2006) 779, 7 December 2006; See also: Commission Staff Working Document accompanying the Interpretative Communication on the application of Article 296 of the Treaty in the field of defence procurement – Impact assessment, SEC(2006) 1554, Brussels, 7.12.2006

⁹⁹ For a further analysis of the interpretative communication, see: Georgopoulos A., 'The Commission's Interpretative Communication on the Application of Article 296 EC in the Field of Defence Procurement', (2007) 16(3) PPLR NA43

¹⁰⁰ Georgopoulos A., 'The European Defence Agency's Code of Conduct for Armament Acquisitions: A Case of Paramnesia?', above fn.37, p.64

invoke the exemption. Moreover, uncertainty remains between the subject matter coverage of the Code of Conduct and that of the proposed Defence Procurement Directive, especially because of the unsettled boundary of the Art.296 EC exemption, which is supposed to delimit the border between the two instruments. For instance, it is unlikely that the exemption can apply to contracts the value of which is only slightly above €1 million, as this will often be too low to concern the essential security interests of a Member State (and would therefore be ruled by the proposed Defence Procurement Directive), but the Code of Conduct is said to also apply to such contracts when the exemption is invoked.¹⁰¹

These misgivings are potentially warranted, and some form of institutional rivalry between the Commission and the EDA may not be excluded, but only the publication of the Defence Procurement Directive will clarify that point. The scope and applicability of the latter will be critical, as compared not only to the Code of Conduct, but also to the Public Sector Directive. One should not forget that one of the likely reasons why the Commission has only been indirectly involved in the EDA initiatives is that many EU Member States have been reluctant to involve it in defence matters.¹⁰² This could potentially hinder the Commission's plans for a Defence Procurement Directive. However, at least from a principle point of view, the initiatives of both institutions seem for now to be complementary¹⁰³:

- The Commission interpretative communication clarifies its views on when the Art.296 EC exemption could be invoked. Even though the use of that exemption remains the privilege of the EC Member States, this document clarifies in which circumstances the Commission may wish to take legal actions against the Member States should they, in its view, misuse the exemption;
- When the Art.296 EC exemption is rightfully invoked by a Member State, the voluntary intergovernmental regime adopted by the EDA should be used for that procurement. Failure to do so would be subject to the peer review system of the Code of Conduct;

¹⁰¹ Georgopoulos A., 'The European Defence Agency's Code of Conduct for Armament Acquisitions: A Case of Paramnesia?', above fn.37, at pp.57 and 62-63

¹⁰² Vlachos K., 'Safeguarding European Competitiveness – Strategies for the Future European Arms Production and Procurement', above fn.72, Chapter 3.C.I

¹⁰³ See also Schmitt B. (rapporteur), 'Defence Procurement in the European Union – The Current Debate', above fn.1, pp.47 et.seq.; Valasek T., 'EU Wants More Defence Competition, Lower Costs', above fn.19; Kuechle H., 'The cost of non-Europe in the area of security and defence', above fn.2, §4.2, but arguing that this would only be the case if the whole range of instruments are coherent

- When an EC Member State would not wish or cannot invoke the Art.296 EC exemption for the procurement of arms, munitions or war material, the Defence Procurement Directive would apply, allowing some more freedom in awarding defence contracts than the Public Sector Directive would. This could provide an incentive to the EC Member States not to invoke the exemption and to keep more of their defence procurement within the scope of EC law;
- In cases the Art.296 EC exemption and the Defence Procurement Directive could not apply because the relevant procurement would be outside the scope of both, the Public Sector Directive would apply.

However, this apparent coherence could be undermined by a number of factors, and only time and the substance of the Defence Procurement Directive will tell how much of a hindrance they would be:

- Some types of defence procurement activities (e.g. collaborative procurement of 'hard' defence material, research and technology related to such material, or the procurement of cryptographic material) would still fall outside the scope of each of these regimes and would remain managed through different sets of rules;
- The conditions for the applicability of the Art.296 EC exemption are still legally unclear. The Commission's interpretative communication only clarifies its own views. It remains to be seen, first if the Commission will actively attempt to enforce its views through the ECJ, and second if the latter will be willing to provide clear judicial interpretation of the limits of that exemption. Even if the subscribing Member States would invoke the Art.296 EC exemption in good faith, it is not certain that their view of the scope of that article – or the Commission's, for that matter – will be that of the ECJ. The dividing line between the two regimes is probably also its biggest uncertainty¹⁰⁴;
- This seemingly coherent regime would only be effective if the subscribing Member States attempt to apply in good faith the EDA voluntary intergovernmental regime. Despite a promising start, it remains to be seen if this would be the case, as we have

¹⁰⁴ As acknowledged by the Commission in COM(2005) 626, above fn.18, pp.4-5

seen that the publication of notices is currently unequal between subscribing member States;

- The scope and applicability of the projected Defence Procurement Directive will have to be carefully defined in order, first of all to be sufficiently clear (simply referring to the 1958 List, which is both unpublished and very general, would probably be insufficient for the practitioner), and second not to overlap with the Public Sector Directive, as this would provide an unclear legal framework¹⁰⁵;
- The procurement procedures and processes of the projected Defence Procurement Directive should remain as coherent as possible with the Public Sector Directive in order to avoid confusion, while still being adapted to the specific requirements of ‘hard’ defence procurement.¹⁰⁶ It is submitted that an amendment of the Public Sector Directive to cater for ‘hard’ defence procurement could be a more coherent solution than an entirely new directive that would be adopted independently.

Even if all or most of the issues mentioned above are clarified, the defence procurement practitioner could still be faced with a wide variety of procurement processes depending on the type of procurement and the applicable exemptions, therefore leading to many potential errors or abuses, even if the harmonisation of national defence procurement rules would be improved.

6. Conclusions

The voluntary intergovernmental regime adopted within the EDA is not limited to the Code of Conduct on defence procurement, and has to be seen as an integrated whole comprising not only the Code of Conduct, but also the Code of Best Practices in the Supply Chain, the Framework Arrangement on Security of Supply in case of operational emergency and the agreement on Security of Information. This regime can be qualified as fairly complete, and its operation has seen a promising start, as shown by the initial success of the related Electronic

¹⁰⁵ See further Schmitt B. (rapporteur), ‘Defence Procurement in the European Union – The Current Debate’, above fn.1, pp.26-30; Georgopoulos A., ‘Commission's Communication on the Results of the Consultation Process on European Defence Procurement’, above fn.91

¹⁰⁶ See further Schmitt B. (rapporteur), ‘Defence Procurement in the European Union – The Current Debate’, above fn.1, pp.30-34; Georgopoulos A., ‘Commission's Communication on the Results of the Consultation Process on European Defence Procurement’, above fn.91

Bulletin Board, even though the initial number of contracts awarded to bidders from another EU Member State is quite low.

However, the regime still suffers from some gaps, such as the lack of provisions on ‘longer-term’ security of supply that would ensure the sustained efficiency of the supply chain needed to support defence equipment over their life, or on the harmonisation of offset requirements. It is submitted that the EDA should continue working on these issues if the intergovernmental regime is really to be complete. The EDA Steering Board itself considers that, even though the regime has been generally successful, more needs to be done to increase cross-border bids and contract awards.¹⁰⁷

In addition, as the intergovernmental regime is purely voluntary and non-binding, its effectiveness will be strongly dependent on the willingness of the subscribing Member States to apply it and provide sufficient information on their use of the Art.296 EC exemption, and of the other subscribing Member State to scrutinise such information and apply peer pressure to entice compliance with the regime. Figures from the Electronic Bulletin Board show that the use of the regime after one year of operation is unequal between subscribing Member States.

Moreover, even though the ongoing initiatives of the European Commission in the field of defence procurement could potentially be a perfect complement to the EDA intergovernmental regime, the borderline between the two – namely the conditions of application of the Art.296 EC exemption for defence procurement – is currently unclear, and the actual scope of any Defence Procurement Directive will be decisive in ensuring the coherence of defence procurement law in the EU.

¹⁰⁷ European Defence Agency Press Release, ‘EDA Steering Board Agrees Path to Implementing Defence Industrial Strategy’, Brussels, 25 September 2007

Post-Publication Postscript

This section is not part of the article published in PPLR and is added only for the enlightenment of the reader, in order to cover the most recent developments. It should not be quoted in reference to the article as published in PPLR and is in no way part of it.

1. Commission Proposal for a Defence Procurement Directive

Following the approval of this article for publication, the Commission published its proposal for a Defence Procurement Directive.¹ Unfortunately, the Commission seems to have fallen into a number of the traps lying in its path.

- Contrary to what we advocated in this article, the scope of the proposed Defence Procurement Directive is defined on the basis of the 1958 List,² despite the fact that this list is officially unpublished, and therefore unavailable as a matter of law, in addition to being too general;
- The proposed directive is quite extensive and visibly inspired by the Public Sector Directive. This opens the possibility of the procedures of the Defence Procurement Directive moving away from those of the Public Sector Directive during the legislative process, thereby potentially leading, for instance, to a ‘public sector competitive dialogue’, and a slightly different ‘defence sector competitive dialogue’. This article expressly warned against this risk.

On the positive side, the proposed Directive would also apply when the secrecy exemption of the Public Sector Directive would apply, and to procurement in civilian fields related to the fight against terrorism. Moreover, the directive prescribes that the negotiated procedure with prior publication is to be the default contract award procedure,³ which should satisfy the requirement for more flexibility in the award of defence contracts.

¹ Proposal for a Directive of the European Parliament and of the Council on the coordination of procedures for the award of certain public works contracts, public supply contracts and public service contracts in the fields of defence and security, COM(2007) 766, 5 December 2007

² Ibid., Art.1

³ Ibid, Art.17-20: the restricted procedure or, in specific cases, the competitive dialogue or the negotiated procedure without prior publication may also be applied

The Commission seems to make a major case out of the fact that the proposed directive would take into account security of supply,⁴ but the ECJ already held that security of supply may be used as a contract award criteria.⁵ This is therefore nothing new, but the requirements that a contracting authority may impose to ensure security of supply as listed in the proposed Directive are quite complete.⁶ However, it remains to be seen how practicable it will be for a tenderer to meet these requirements, especially those to secure specific commitments from its national authorities.

2. Commission Proposal an Intra-Community Transfer Directive

The Commission at the same time proposed a directive to simplify the national laws on intra-Community transfer of defence products.⁷ Even though this initiative is only indirectly related to defence procurement law, it has the potential to improve the efficiency of the European defence equipment market.⁸

3. Further Action Plan of the Commission

The Commission published a new strategy document⁹ highlighting additional measures that it plans to investigate in order to strengthen the European defence market. These include promoting the use of common defence standards, investigating an EU system on security of information, studying how to improve the legislation on the control of strategic defence assets, which is up to now entirely national, supporting the pooling of demand and the alignment of procurement planning, promoting the pooling of R&D investment, and continuing to strengthen the position of SME. As the document itself acknowledges, a number of these initiatives are already being purposed by the EDA, and it remains to be seen how the relationship between these two institutions will develop, despite the fact that the EDA

⁴ European Commission presse release, 'Commission proposes enhancing openness and transparency in EU defence markets', MEMO/07/547

⁵ Case C-324/93, *The Queen v Secretary of State for Home Department, ex parte Evans Medical Ltd and Macfarlan Smith Ltd* [1995] ECR I-563, at [44]-[45]

⁶ COM(2007) 766, above, Art.15

⁷ Proposal for a Directive of the European Parliament and of the Council on simplifying terms and conditions of transfers of defence-related products within the Community, COM(2007) 765, 5 December 2007

⁸ See Unisys study, 'Intra-Community Transfers of Defence Products', Brussels, February 2005

⁹ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: 'A strategy for a stronger and more competitive European defence industry', COM(2007) 764, 5 December 2007

welcomed the Commission efforts and qualified them as complementary to its own initiatives.¹⁰

4. Additional Clarification from the EDA on the EBB

The EDA also clarified that the main reason why only a limited number of defence contracts were awarded to a bidder from another country (about 15% at the time of our analysis, see above §4.3) was because about 80% of the bids received by the defence contracting authorities were from companies within their national borders.¹¹ This is important information, as it shows that the efforts of the EDA should concentrate first of all on initiatives to stimulate cross-border tendering. There could be more issues with the drafting of the tender documents and the bidding process than with the actual contract award.

¹⁰ EDA press release, 'EDA Welcomes Commission Communication on EU Defence Industry and Market', Brussels, 5 December 2007

¹¹ Cowan G., 'Interview: Nick Witney, Chief Executive Officer of the European Defence Agency', Janes Defence Weekly, 26 September 2007, p.34