

Chaillot Papers

August 2003

n° 63

The European Union and armaments

Getting a bigger bang for the Euro

Burkard Schmitt



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Burkard Schmitt

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Like a hackneyed news item, the idea of creating a European armaments agency has continually haunted the process of building European defence. Already at Maastricht in 1992 it was included in annexes to the Treaty (in the form of a WEU declaration). It has now been spelt out in full in the draft Constitutional Treaty proposed by the Convention in June 2003. Even better, at the European Council in Thessaloniki, heads of state and government decided to accelerate the process of creating such an agency, from 2004, independently of the results of the forthcoming IGC. Whatever the reasons for this haste – genuine urgency or negotiating tactic – one is bound to be satisfied with the importance now attached to the armaments dimension of European security and defence policy.

One also notes with a certain interest two coincident developments. Top-down, there is the decision by heads of state to give the Union ‘an overall strategy in the field of foreign and security policy’ based on a common definition of the Union’s interests and principles of action and on a common evaluation of the threats and possible responses to them. This suggests that it was not considered possible for the CFSP and ESDP to remain at the level of ad hoc interventions, but that a quantum leap in the consistency of the Union’s external actions had become necessary. Bottom-up, there is the decision to create ‘an intergovernmental agency in the field of defence capabilities development, research, acquisition and armaments’, indicating that the emphasis put on the Union’s military capabilities since Cologne risked producing little in the way of results if, even before looking at military instruments, the same serious attention were not paid to technological and industrial capacity.

What type of agency is therefore required and for what type of market? Those are the two technically difficult and politically sensitive questions addressed in this Chaillot Paper by Burkard Schmitt, assistant director and research fellow at the Institute. Following publication of Chaillot Paper 59 in May this year, a volume containing core documents on armaments, this essay by Burkard Schmitt on the one hand sketches the broad lines of a possible European armaments market. On the other it clarifies the issues involved, the constraints, the modalities and the functions of a European agency that will have real capabilities provided member states seriously agree to reconcile their national constraints with the aim of greater cost-effectiveness.

The traditional obstacles will of course weigh heavily in this: the power of bureaucracies, the role of national sovereignty vis-à-vis the Commission, the

priority given to the transatlantic dimension or Europe, the widely differing industrial and financial potential of member states concerning armaments, etc. There is already a hint of these various constraints in the options for setting up the future agency being unofficially discussed: will its function be more conceptual, concerned with the exchange of information and discussion of possible cooperative projects, or will it go further and have a more operational, more directive function that therefore places more constraints on member states? Is the agency's area of competence to be limited and based on the needs of ESDP in the strict sense, i.e. on the capabilities identified in the Headline Goal, or will it actually have more general competence? Will the agency's missions cover all dimensions of procurement – early identification of requirements, research, development, cooperation, acquisition and structure of the market – or will it take a more selective approach? How much flexibility will be needed to ensure the agency's viability given the constraints of unanimity at 25?

There seems little doubt that it is legitimate to pose such questions, given member states' national political constraints. Moreover, they have always affected the various efforts made in the last ten years to improve armaments cooperation (OCCAR, LoI, WEAG, etc.). The problem is precisely that these traditional efforts at cooperation have produced very little in the way of results. If the aim is to maintain an industrial capacity and acquire the necessary military capabilities, the time has perhaps come to consider methods that are more innovative and better suited to European convergence. Are member states ready to make that quantum leap?

Paris, July 2003

The proposals of the Convention on the Future of Europe and the recent European Commission Communication on a Defence Equipment Policy have revived the debate about the EU's possible involvement in armaments. There is indeed a chance today that a European Agency for Armaments, Research and Capabilities will be set up and anchored in the new EU Treaty. At the same time, there is a growing consensus that the EU Commission should have certain competencies in the field of security-related research, and even the establishment of a common defence equipment market is (again) under discussion.

There are several reasons for this new openness vis-à-vis the EU's involvement in armaments. First of all, the development of ESDP has changed the political environment and prepared the ground for the current debate. At the same time, the growing internationalisation of defence-related companies has transformed the industrial landscape and created the need for new regulatory frameworks. Last but not least, persisting budgetary constraints oblige European governments to go beyond current arrangements and to envisage more comprehensive and cost-efficient solutions.

Up until now, the debate on armaments in the EU has remained vague and general, and the new openness might easily dissipate once discussions get more concrete. However, an in-depth discussion of the details cannot be avoided, and there is a need to clarify what the various proposals that are on the table could actually mean in practice.

The purpose of this *Chaillot Paper* is therefore twofold. First, it explains the importance of armaments and its specific problems, describes the current state of play and develops possible solutions for the future. Such a comprehensive approach seems appropriate, in particular since armaments is a highly complex field in which neither political leaders nor the public normally take a strong interest. However, the stakes are too high, in particular for European taxpayers, to leave the issue exclusively to a closed circle

of procurement experts. A broader debate on the reform of Europe's armaments sector is therefore desirable, and this paper is intended as a contribution to it.

The second, even more important objective of this *Chaillot Paper* is to take the debate one step further and to develop a clearer idea of how to implement the various initiatives that are currently under consideration. There is in fact much talk, in particular about an Agency, but very little conceptual thinking yet. The present essay attempts to start filling this gap. In this context, its focus is on the future Armaments, Research and Capabilities Agency, because the time schedule for its creation is more pressing than the one for the establishment of a defence equipment market.

The paper is therefore divided into three parts. The first chapter presents the background of the current debate. It illustrates why it is so difficult to arrive at a common armaments policy, explains the necessity to act and describes the areas in which reforms are needed. It shows why the EU could be an appropriate framework for action, and ends with an overview of the recent initiatives aimed at bringing the subject of armaments into the EU.

The second chapter presents an analysis of existing initiatives and bodies, both inside and outside the EU framework. Such an assessment is particularly important since any new structure should (a) draw on the experience of existing armaments cooperation forums, (b) incorporate useful elements and (c) interact with other bodies and policies related to armaments.

The third chapter is the key element of this paper. Drawing on an analysis of existing institutions and policies, it develops concrete proposals for action. It is divided into two parts. The first presents a possible blueprint for the future Armaments, Research and Capabilities Agency and shows how it should ideally be constituted and work. The basic assumption here is that the Agency must be strong and efficient enough to have a real impact on Europe's armaments sector. The second part of the chapter deals with market issues. It presents an outline for a European Defence Equipment Market based on Community law and gives some indication of how it could be formed.

Towards a common armaments policy?

Difficulties and necessities

Up until now, armament has traditionally been a national domain. In Europe, the production, trade and procurement of military goods and services have been deliberately excluded from the European integration process by EU member states, which have preferred to keep these activities under national control. That policy has been legally based on Art. 296 (ex Art. 223) of the Treaty establishing the European Community (TEC), which allows member states to derogate from treaty rules where they can demonstrate that their essential security interests are at stake.¹

National governments have traditionally defined these 'security interests' very broadly in order to override the disciplines of Community policies in the field of armaments. At the same time, member states have refused to use the intergovernmental framework of Common Foreign and Security Policy (CFSP) for armaments cooperation. Some structures for doing this exist outside the EU, but member states have neither transferred national sovereignty to European institutions nor developed a systematic coordination of their national policies. There are several reasons for this:

- Armaments policy is mainly a function of other policies, in particular defence, security and foreign policy. As long as these policies remain mainly national, a common armaments policy is extremely difficult to agree on: military strategies and concepts differ, which makes harmonisation of military requirements a thorny task; regional policies diverge, which leads to different arms export practices; alliance concepts vary, which leads to diverging armaments cooperation schemes and industrial strategies, etc. Since the CFSP and even more so its military dimension (ESDP) are comparatively recent and modest endeavours, progress in the field of armaments has been almost inevitably slow and painful.

1. Article 296 reads as follows: '1) The provisions of this Treaty shall not preclude the application of the following rules: a) no Member State shall be obliged to supply information the disclosure of which it considers contrary to the essential interests of its security; 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 the trade in arms, munitions and war material; such measures shall not adversely affect the conditions of competition in the common market regarding products which are not intended for specifically military purposes. 2. The Council may, acting unanimously on a proposal from the Commission, make changes to the list, which it drew up on April 1958, of the products to which the provisions of paragraph 1 b) apply.' Quoted in Burkard Schmitt, 'European armaments cooperation - Core documents', *Chaillot Paper 59* (Paris: EU Institute for Security Studies, April 2003), p. 10.

- ▶ Political divergences have been – and still are – reinforced by different industrial interests. The bulk of the defence industries and their funding is concentrated in the United Kingdom, France and – to a lesser degree – Germany. These three countries, together with Italy, Spain and Sweden, represent more than 90 per cent of Europe’s defence industrial capabilities, 85 per cent of EU defence spending and 98 per cent of all R&D expenditures. As arms producers, they inevitably have different procurement and market policies than their European partners who have no or only minor defence industrial capabilities and often buy their military equipment in the United States.
- ▶ Europe’s arms-producing countries, however, do not represent a homogeneous group either. Due to their different historical backgrounds and political aspirations, each of them has a very specific interpretation of (a) the function of armaments for its foreign, economy, industrial policies, and (b) the role governments should play as customers, regulators, sponsors and shareholders vis-à-vis defence industries. This, in turn, leads to important divergences on defence-related trade, procurement and industrial issues (European preference, exports, competition, access to the US market, etc.).
- ▶ Defence industries have not always been a driving force behind far-reaching reforms either. Even in aerospace and defence electronics, where international cooperation has been common practice for several decades, mutual rivalry and mistrust between national champions were rather the rule than the exception and reinforced national egoisms at the political level. This situation improved only recently, when industrial consolidation crossed national borders and governments started to behave more like ‘normal’ customers. However, sectors and companies that are not competitive still fear the opening up of defence markets and the loss of national protection.

The consequences of all this are well known: Europe’s armament sector has remained fragmented into national markets, with costly duplication in all armaments-related areas (procurement bureaucracies, research activities, industrial capacities and defence programmes).

Ironically, armaments cooperation has often made things even worse. Organised traditionally on a purely intergovernmental and ad hoc basis, cooperative projects have implied complex institutional and industrial settings, creating delays and extra costs. The

juxtaposition of separate ad hoc structures for each project has implied considerable overhead costs, whereas potential cost-savings have remained unexploited due to rigid interpretation of *juste retour*² and considerations of security of supply. Cooperative schemes have been particularly inefficient, since all the major arms-producing countries have tried to build up and maintain their own development and production capabilities in as many technologically interesting fields as possible. In consequence, participation has often varied from project to project, and the division of labour has been defined in such a way that all participants have been included in work on all interesting components. This, in turn, has led to additional over-capacities and redundancies.³

Since the end of the Cold War, the costs of such fragmentation have become unbearable. On the one hand, development costs of complex weapon systems have increased dramatically and started to exceed the financial means of even the big European countries. At the same time, the restructuring of armed forces and the growing number of crisis management operations have created additional costs, reducing in particular the part of defence budgets devoted to investment. On the other hand, European defence expenditure was in constant decrease throughout the 1990s. The rate of decline has slowed down since 1995, but the trend was not reversed until recently, and then only in a few EU member states.⁴ 'The main reasons for this are well known, from the rigidity of fiscal policies to the social and demographic structure of European societies, to the deeper-seated reluctance of governments to invest in military capabilities in the absence of any tangible [military] threat.'⁵ Neither the wars in the Balkans nor the terrorist attacks of 11 September 2001 have changed that picture. Last but not least, the general crisis of public finance in most European countries and the limits on government deficits set in place by the Growth and Stability Pact make it highly unlikely that we shall witness much of a change in the near future.

The discrepancy between flat, stagnating investment budgets and increasing costs has had a damaging effect in two respects. First, it has resulted in glaringly obvious gaps in Europe's military capabilities. As the interventions in Kosovo and Afghanistan demonstrated, European armed forces are inadequately equipped for modern warfare. Indeed, Europe's military shortcomings are now such that ESDP is in danger of remaining a paper tiger. Second, the limits on military spending are increasingly damaging

2. According to the *juste retour* (fair return) principle, the industry of each participating nation should get a work share that corresponds to the financial contribution of its government. In its traditional form, industrial *juste retour* is calculated each year, programme by programme. In practice, this method has greatly reduced the flexibility of programme management and has often led to an inefficient distribution of work.

3. See Joachim Rohde and Markus Frenzel, 'Transatlantic Gaps and European Armaments Co-operation - Optimising European Resource Allocation', in *Prospects on the European Defence Industry* (Athens: Defence Analysis Institute, 2003), p. 80.

4. In the aftermath of 9-11, some of the most important European defence spenders announced increases in their defence spending: In the United Kingdom, the three-year comprehensive spending review from July 2002 promised a defence budget increase of £3.2 bn from £29.33 bn to £32.78 bn between 2002/2003 and 2005/2006. In France, the new *Loi de Programmation militaire* for the period 2003-2008 envisages in particular an increase of the equipment budget to an average of €14.5 bn per year for the period 2003-2008. Italy has pledged to increase defence spending over the next 10 years to 1.5 per cent of its GDP. Germany, in contrast, has announced that it is maintaining its defence budget at €24.6 bn until 2006. However, whether increases that have been announced are actually made will certainly depend on overall economic results in each country. See *The Military Balance 2002•2003* (Oxford: Oxford University Press for the IISS).

5. Antonio Missiroli and Burkard Schmitt, 'More €uros for European Capabilities', in *European Voice*, 27.6. - 3.7.2002.

the European Defence Industrial and Technological Base (EDITB). Lack of investment in research in particular is seriously jeopardising industry's technological ability to prepare for the future. At the same time, European companies find it increasingly difficult to compete with the big American defence groups, who benefit from an enormous, well-protected domestic market and a growing US defence budget.⁶

All this has put European countries under pressure to develop a more ambitious and systematic approach towards armaments cooperation. Throughout the 1990s there were a multitude of multinational initiatives at different levels and with varying memberships, leading to an extremely complex institutional landscape. Most of them, in particular WEAG, WEAO, OCCAR and the LoI, developed outside the EU framework, but the EU has also gained some competences in areas that are at least indirectly related to armaments (dual-use items, civil hi-tech research, arms exports, military capability needs).

Some of these initiatives are innovative and promising. In general, however, results have not been satisfying. Market fragmentation and duplication persist, and the institutional setting remains a patchwork. In some areas competences overlap, whereas others are not covered at all. The various initiatives are not coordinated, and there is no overall strategy, because there is no coherent armaments policy.

Europe will have to develop a much more efficient approach if it wants to equip its armed forces adequately and sustain a competitive EDITB. What is needed is a coherent framework for a consistent policy in several areas:

- **Defence Procurement.** In the future, military operations will normally be conducted within multinational coalitions. In consequence, interoperability of European armed forces will be key. To be economically beneficial, this should be translated into common defence equipment programmes with common technical characteristics and procurement schedules. What is therefore needed is a European procurement system that allows for both more and better cooperation. This, in turn, will only be possible if there is, finally, an efficient harmonisation of military requirements and better programme management. In addition, common acquisition of non-military goods could generate considerable economies of scale.

6. In 2001, the United States (DoD only) spent more than twice as much on defence as all 15 EU members together. With an increase in US defence spending of \$48 bn for FY 2003, and further increases planned from \$396.8 bn in 2003 to \$469.8 bn in 2007, the transatlantic financing gap will continue to grow over the next years.

- ▶ **Defence Research.** It is well known that Europe spends too little on military research. Moreover, only a small proportion of this money is spent on European cooperation. This means that far better coordination is indispensable within the field of military research. At the same time, the somewhat artificial distinction between civil and military research should be overcome in order to allow full exploitation of potential synergies. This will imply a new institutional setting and a redefinition of competencies among the different actors in this field.
- ▶ **Defence equipment market.** The fragmentation of regulatory frameworks governing defence-related activities at the national level is a major cause of inefficiency. The creation of a common European Defence Equipment Market (EDEM) with a single set of rules and regulations would therefore be a major step forward. A fully integrated EDEM would imply, *inter alia*, common procurement and competition rules, simplification of intra-European transfers, a common security of supply regime, harmonisation of security regulations and a common export regime. This would create a homogeneous defence economic space, allowing transnational defence companies (TDCs) to rationalise their internal organisation in an economically efficient way. At the same time, the establishment of an EDEM would increase Europe-wide competition, encouraging those industrial sectors that are still nationally focused to consolidate across national borders. On top of that, enhanced competition and streamlined regulatory frameworks would generate considerable cost-savings.

Ideally, policies in all three areas should be shaped on the basis of a common definition of 'strategic' industrial interests. Procurement choices, research investments and market decisions can only be consistent if there is a common understanding of the strategic importance of the various military, technological and industrial capabilities. The question is in which areas and at what level European countries want, *for strategic reasons*, to maintain industrial and technological capabilities (e.g. national level for nuclear weapons and European level for fighter aircraft), and which can simply be left to international competition?

Establishing a coherent framework and implementing a common policy for armaments will be enormous challenges for European states who, on the one hand, recognise the need for greater

cost-effectiveness, but, on the other, are reluctant to give up national prerogatives. From a purely economic point of view, the most efficient solution would be to 'communitarise' armaments, i.e. to create a single defence market and replace national research and procurement agencies by supranational organisations. Since this is politically unacceptable to member states, the only way to make progress is to improve the intergovernmental method, to introduce at least some integrated elements into the procurement cycle and to use Community instruments wherever possible. What is sure, however, is that only a comprehensive approach, based on a consistent long-term strategy and making use of different instruments, will be able to cope effectively with the challenges of budget constraints, cost increases and structural inefficiencies.

The EU – a framework for action?

At least in theory, the EU is an appropriate framework for developing and implementing such an approach. First of all, an EU armaments policy would be a natural complement to ESDP. From a political point of view, this could help to reduce divisions between arms-producing and non-producing countries. From a practical point of view, the EU military bodies and a reformed European Capabilities Action Plan (ECAP) process (see below) could play a useful role in the early stages of the procurement cycle, by developing common concepts, doctrines and capability needs as key elements of the harmonisation of military requirements. Moreover, the EU offers the possibility to use both first- and second-pillar instruments. This in turn allows combining the creation of a common defence market and the establishment of a common procurement system. At the same time, a cross-pillar approach would help to develop and implement a comprehensive strategy for strategic industries. Last but not least, the EU could negotiate with the United States on arms trade issues and would be a much more powerful interlocutor than individual member states.

Since the development of ESDP in general, and the ECAP experience in particular, there is indeed a growing consensus that at least certain functions of armaments policy should be brought into the EU framework. However, at the political level, important stumbling blocks persist: the big arms-producing countries still diverge on procurement philosophies and industrial strategies.

Moreover, security of supply, the involvement of the Commission and relations to third parties, in particular the United States, remain highly controversial. At the same time, non-producing countries, which often buy American rather than European weapon systems, do not necessarily recognise the importance of a European armaments policy. On top of that comes the growing diversity of interests in a Union at 25, which makes the prospects for CFSP and ESDP somewhat uncertain and might thereby shatter the perspectives for an EU armaments policy.

Difficulties can also come from institutional stakeholders, namely national procurement bureaucracies. On the one hand, they are (almost) the only ones with the necessary expertise to develop common European armaments structures. On the other, they are not renowned for producing experts with an international mindset who are willing to break with traditional approaches. Moreover, they would act against their own best interests as administrations if they developed an ambitious concept implying the far-reaching transfer of competencies to the European level. Bureaucratic inertia, if not resistance, can become a real problem, in particular since political leaders do not normally take a particular interest in armaments matters.

Military and financial arguments will hopefully be strong enough to overcome these obstacles: no matter how CFSP and ESDP develop, it remains a fact that future military operations will normally be multilateral, and that standardisation of equipment will become ever more important. Moreover, in Europe the gap between rising costs and limited budgets will persist or even worsen. This is not only a problem of severely reduced budgets, but also of structural change: since most European armed forces have been streamlined and downsized, national markets are in general too small today to generate adequate economies of scale. For most complex weapon systems, per-unit costs will simply be too high if the production run is limited to the needs of a single European country. National reforms will therefore not be enough to cope with these problems. In other words, European countries simply have no choice: even without a fully-fledged CFSP/ESDP, they will have to dare a quantum leap in armaments cooperation if they want to maintain a noteworthy defence industrial base and capable armed forces. However, the extent to which the EU becomes the framework for this quantum leap remains to be seen.

The outcome is still unclear, but the debate on EU involvement in armaments is now open. Three initiatives will structure the discussion: first, the Commission's Communication on a European Defence Equipment Policy, adopted 11 March 2003,⁷ second, the provision for the creation of an EU Agency included in the Convention's draft Treaty establishing a Constitution for Europe,⁸ and third, the Presidency Conclusions of the Thessaloniki summit of 19-20 June 2003.⁹

In its Communication, the European Commission suggests a common armaments policy, based on both Community and CFSP instruments. A cross-pillar approach would be possible within the provisions of the current treaties and should address defence equipment demand, supply, market and research. The Communication focuses on the establishment of a European defence equipment market and research policy as the two areas where 'Community action is most likely to be able to add value'.¹⁰ In both areas, the Commission presents proposals for action.

As to research, the Commission suggests identifying a 'European agenda for advanced research relating to global security and the most appropriate ways of tackling it jointly. To prepare for the implementation of this advanced research agenda, the Commission [will] launch a preparatory [action] . . . to implement some specific aspects that would be particularly useful in carrying out Petersberg tasks.'¹¹

Concerning a defence equipment market, and the politically 'hot' issues in particular, the Commission is cautious enough not to propose solutions, but only to announce further analysis and reflection.

- Procurement law.** The EC will issue an Interpretative Communication by the end of 2003 on the implications of recent court judgements, especially with regard to the definition of the scope of Article 296. In parallel, it will work on a Green Paper, which might be issued in 2004 as a basis for discussion with stakeholders.
- Intra-Community transfer.** In 2003, the EC will launch a study on the impact of Community-level legislative initiatives, and, depending on its results, at the end of 2004 start elaborating the appropriate legal instrument.
- Competition.** The EC will continue its reflection on the application of competition rules in the defence sector, taking due

7. Reproduced in Burkard Schmitt, *op. cit.* in note 1, pp. 162-80.

8. http://european-convention.eu.int/doc_register.asp?lang=EN&Content=DOC.

9. <http://ue.eu.int/newsroom/makeFrame.asp?MAX=&BID=76&DID=76279&LANG=2&File=/pressData/en/ec/76279.pdf&Picture=0>.

10. Commission Communication, p. 168.

11. *Ibid.*, p. 176.

account of the specificities of this field and the provisions of Article 296 TEC.

- **Dual-use items.** The EC will, in the relevant Council working bodies, raise the issue of the Commission's involvement in export controls regimes.

Published in the run-up to the next Intergovernmental Conference (IGC), this Communication represents a strong political signal to member states that the Commission is ready to contribute with its expertise on industrial and market issues to a possible EU defence equipment policy. At the same time, the various initiatives define a 'road map' for further discussions on the establishment of a common defence market.

The second relevant document is the Convention's draft Treaty establishing a Constitution for Europe. According to Article I-40.3 of the draft Treaty, 'a European Armaments, Research and Military Capabilities Agency shall be established to identify operational requirements, to promote measures to satisfy those requirements, to contribute to identifying and, where appropriate, implementing any measure needed to strengthen the industrial and technological base of the defence sector, to participate in defining a European capabilities and armaments policy, and to assist the Council of Ministers in evaluating the improvement of military capabilities.'¹²

Article III-207 specifies that the Agency, 'subject to the authority of the Council of Ministers, shall have as its task to:

- contribute to identifying the Member States military capability objectives and evaluating observance of the capability commitments given by the Member States;
- promote harmonisation of operational needs and adoption of effective, compatible procurement methods;
- propose multilateral projects to fulfil the objectives in terms of military capabilities, ensure coordination of the programmes implemented by the Member States and management of specific cooperation programmes;
- support defence technology research, and coordinate and plan joint research activities and the study of technical solutions meeting future operational needs;
- contribute to identifying and, if necessary, implementing any useful measure for strengthening the industrial and technological base of the defence sector and for improving the effectiveness of military expenditure.

12. <http://european-convention.eu.int/docs/Treaty/cv00820-re01.en03.pdf> (27 June 2003) Part I-40.3.

[According to the draft Treaty,] the Agency shall be open to all Member States wishing to be part of it. The Council of Ministers, acting by qualified majority, shall adopt a European decision defining the Agency's statute, seat and operational rules. That decision should take into account of [sic] the level of effective participation in the Agency's activities. Specific groups shall be set up within the Agency, bringing together Member States engaged in joint projects. The Agency shall carry out its tasks in liaison with the Commission where necessary.¹³

If approved by the IGC, this article would become part of the new EU Treaty, which is planned to enter into force in 2007/2008. However, this schedule was confused when the European Council of Thessaloniki decided at the end of June 2003 to task 'the appropriate bodies of the Council to undertake the necessary actions towards creating, *in the course of 2004* [emphasis added], an inter-governmental agency in the field of defence capabilities development, research, acquisition and armaments. This agency, which shall be subject to the Council's authority and open to participation by all Member States, will aim at developing defence capabilities in the field of crisis management, promoting and enhancing European armaments cooperation, strengthening the European defence industrial and technological base and creating a competitive European defence equipment market, as well as promoting, in liaison with the Community's research activities where appropriate, research aimed at leadership in strategic technologies for future defence and security capabilities, thereby strengthening Europe's industrial potential in this domain.'¹⁴

This means that one of the provisions of the new EU Treaty would be implemented even before it is ratified and entered into force. This approach seems legally and politically somewhat dubious, but it shows that member states are apparently determined to obtain concrete results as soon as possible.

However, for the time being there is still no clear concept of the future Agency. The Constitution's draft Treaty and the Presidency's Conclusions give a broad definition of its missions, but they do not say anything about the organisation and functioning of the Agency.¹⁵

Ambiguity might be helpful in launching the project, but it also entails political risks. The devil is in the detail, and it will probably be difficult to agree at 25 on the Agency's statutes. The

13. <http://european-convention.eu.int/docs/Treaty/cv00848.en03.pdf> (9 July 2003) revised part III of the draft.

14. Presidency Conclusions, Thessaloniki summit 20 and 21 June 2003, para. 65, p. 19, available at <http://ue.eu.int/newsroom/makeFrame.asp?MAX=&BID=76&DID=76279&LANG=2&File=/pressData/en/ec/76279.pdf&Picture=0>.

15. The various contributions that were made in the course of the Convention's discussions remained vague as well. Key contributions are: Joint proposals by Dominique Villepin and Joschka Fischer, Prague, 21 November 2002, reproduced in Jean-Yves Haine, 'From Laeken to Copenhagen – European defence: core documents, *Chaillot Paper 57* (Paris: EU Institute for Security Studies, February 2003), pp. 214-8; Final report of the Defence Working Group, Brussels, 16 December 2002, *ibid.*, pp. 249-63; The Franco-British Declaration on Strengthening European Cooperation in Security and Defence, Le Touquet, 4 February 2003, available at <http://www.elysee.fr/actus/dep/2003/province/02-frgb-touquet/angdefsecu.htm>. It is worth noting, however, that these contributions differ greatly as to the scope and nature of the Agency.

moment of truth will come, and it is high time to develop a clearer idea of the Agency, its institutional linkages, structures and rules.

According to the different contributions made to the Convention, the Agency should be based on the experience of existing bodies and incorporate at least some of them. This makes sense in order to avoid the risk of reinventing the wheel and/or merely adding additional layers to an already complex institutional landscape. The first step towards a clearer concept, therefore, is an assessment of what already exists and the lessons to be learnt, and identification of elements that could be used for any new structure.

What exists

Outside the EU framework

WEAG/WEAO

The Western European Armaments Group (WEAG) is the traditional forum for armaments cooperation in Europe. Its origins date back to 1976, when the defence ministers of European NATO countries (except Iceland) established a first forum for armaments cooperation, the Independent European Programme Group (IEPG). In December 1992, IEPG functions were transferred to WEU, and WEAG was created. Since then, the number of WEAG member states has increased from 13 to 19, and includes non-NATO EU members. The general objectives of the WEAG are: more efficient use of resources, in particular through better harmonisation of requirements; opening up of national defence markets to cross-border competition; strengthening of the European defence technological and industrial base; and cooperation in research and development. According to the WEAG's principles, all member countries are entitled to participate fully and with the same rights and responsibilities in any European armaments cooperation activity. To avoid duplication, however, there should be a single European forum for armaments cooperation.¹⁶

Within the WEAG framework, ministers of defence meet once a year, National Armaments Directors (NADs) every six months. Between these meetings, continuity is provided by a staff group consisting of the Permanent Representatives of the NADs in Brussels. WEAG's work is organised in three panels.

- The objective of Panel I is to promote cooperative equipment programmes. It compares WEAG nations' armaments replacement schedules, which are collated and presented in an annual document. Where cooperation is considered possible, sub-groups involving the collaborating nations can be established in order to harmonise requirements through the development of Feasibility Studies and European Staff Requirements. To

16. For a general overview, see <http://www.weu.int/weag/index.html>. For a more detailed discussion, see Andrew D. James, *The Current State of European Cooperation in the Field of Armaments* (Rome: CeMIS (Military Centre for Strategic Studies), 2003).

conduct the development and production phases, a project group can follow up the work of the subgroups.

- The mission of Panel II is to strengthen cooperation in defence research and technology (R&T). To achieve this objective, WEAG has organised its R&T activities around 13 so-called CEPAs (Common European Priority Areas). Not all CEPAs are equally active; the success of a CEPA depends in fact to a large extent on the enthusiasm of members and the quality of its chairman. WEAG's main instrument for R&T has been the European Cooperation for the Long Term in Defence (EUCLID) Programme, involving industry and research institutes.¹⁷ Under EUCLID rules, projects must be notified to Panel II for formal approval. However, the Panel has almost no power to influence the choices made by its members on the establishment of projects. In May 2001, WEAG defence ministers signed another MOU, called EUROPA.¹⁸ EUROPA is a general umbrella allowing participants to develop certain rules on their own, with greater flexibility in particular for Intellectual Property Rights (IPRs).
- Panel III deals with basic aspects of a common defence economic policy and armaments cooperation procedures. Panel III has developed a set of principles for WEAG-wide armaments activities, laid down in the Coherent Policy Document (CPD), which was approved by defence ministers in 1990 and updated in 1999. The CPD explicitly states that, during a transition period, application of the *juste retour* principle and support for countries with developing defence industries (DDIs) are two important aspects of the creation of a European Defence Equipment Market (EDEM). To foster cross-border competition and industrial cooperation, focal points for procurement issues have been established in all WEAG countries. Each focal point publishes its country's defence procurement needs in national bulletins, which are available WEAG-wide to inform industry and procurement authorities on future national defence requirements.¹⁹

In 1993 WEAG established an Ad Hoc Study Group (AHSG) to review the possibilities of creating a European Armaments Agency (EAA). In the absence of the necessary political, legal and economic conditions, the group did not recommend creation of a fully-fledged EAA at that time. However, based on the work of the AHSG, in 1996 WEAG defence ministers established the Western

17. Spontaneous proposals from industrial consortia can be taken into consideration through a mechanism called EUROFINDER. A third programme, THALES, aims at facilitating cooperation between government research establishments.

18. 'European Understandings for Research Organisation, Programmes and Activities', reproduced in Burkard Schmitt, *op. cit.* in note 1, pp. 95-107.

19. For an analysis of WEAG Panel III see Sandra Mezzadri, 'L'ouverture des marchés de la défense : enjeux et modalités', *Occasional Paper 12* (Paris : Institute for Security Studies of WEU, February 2000), pp. 10-14.

European Armaments Organisation (WEAO). As a subsidiary body of WEU, the WEAO shares the latter's international legal personality and can therefore offer a legal framework for armaments cooperation.²⁰

Although the WEAO Charter provides for a broad range of potential activities,²¹ WEAO has operated only as a Research Cell, providing member states with a variety of services in the field of military research and technology: Some are common services provided to all members, including administrative support to the WEAO Board of Directors and WEAG Panel II, while others concern specific groups of countries undertaking cooperative R&T projects (contractual assistance in the preparation of project arrangements, letting contracts).

After the establishment of WEAO, discussions on a fully-fledged Armaments Agency continued. Following the ministerial meeting in Erfurt in November 1997, a so-called 'Masterplan' was worked out, defining the necessary steps on the path to an EAA. A Group of National Experts (GNE) was established in order to develop the rules and regulations, as well as the structure for the EAA, so as to allow ministers to decide in 2001 about implementation of the Agency. In the following years, proposals covering the functions of the EAA, the principles and policies governing these functions, a generic structure and organisation charts for the build-up and fully-fledged phases of the EAA with additional supporting documents were drafted, discussed and presented to WEAG NADs.

At their meeting in Rome on 16 May 2002, ministers formally endorsed the concept of an evolutionary process, envisaging the establishment of an EAA as soon as all appropriate conditions had been met and political consensus reached. Any remaining work should continue under the direction of the NADs. In reality, however, this was the end of the project. The GNE was dissolved, and national governments showed no interest in the recommendations made in the Masterplan. There was apparently no longer any political will to establish the EAA within the framework of WEAG.

The inglorious end of the Masterplan is indicative of WEAG's weakness and declining relevance. Since its creation, it has suffered from a lack of both interest and political support from national authorities. Consequently, WEAG has never become more than a forum for discussion. Consensus-based decision-making has allowed only for agreements on the basis of the lowest

20. For an overview, see <http://www.weu.int/weao/site/fr/ameset.htm>.

21. According to Article 6 of the WEAO Charter, 'the aim of WEAO is to assist in promoting and enhancing European armaments co-operation, strengthening the European defence technology base and creating a European defence equipment market.' In order to carry out this aim, 'the WEAO may undertake, in the name of the WEU and on behalf of one or more participants, the following functions: a) defence research and technology activities; b) procurement of defence equipment, c) studies, d) management of assets and facilities, e) other functions necessary to carry out the aim of the Organisation' (Article 7). See Burkard Schmitt, *op. cit.* in note 1, p. 12.

common denominator. The principle that all WEAG members should be entitled to participate with the same rights and responsibilities in any armaments cooperation forum has pushed the main arms-producing countries into setting up other institutional arrangements that allow for greater flexibility and exclusiveness (thereby undermining another WEAG principle, stipulating that there should be a single European armaments cooperation forum and no duplication in this field).

Panel I has suffered from weak structures and low-level participation; Panel II, and WEAO in particular, have had at least limited success, but the Research Cell has remained de facto a pure contracting agency, and the contracts it has let represent only 2.5 per cent of European military R&T spending. Panel III has been paralysed by continuing divergences on key issues such as *juste retour* and the legally non-binding nature of its documents, which leaves application of the CPD in particular to the political will of member states.

In short, WEAG has addressed the right issues but has lacked the means and structures to find satisfactory solutions. Since the transfer of WEU's main functions to the European Union, WEAG's political relevance has diminished even further. WEAG might continue to exist as a forum for dialogue between EU and non-EU states. However, its functions should be transferred to other, more efficient frameworks inside the EU.²²

What will become important, in contrast, is the EUROPA Memorandum of Understanding (MOU), signed by WEAG ministers in May 2001. EUROPA provides that any two or more signatories can propose the creation of a European Research Grouping (ERG) to carry out either a number of individual R&T projects or a single major programme. Membership of ERGs is variable – depending on who is interested in joining the Grouping, and on who agrees on the content of the ERG arrangement in which the particular rules for that ERG are set out.²³ The first ERG was launched in late 2001, with 14 members. It contains all provisions necessary for the conduct of individual R&T projects. Compared with previous MOUs governing R&T cooperation, ERG No. 1 provides for greater flexibility: two or more ERG members can agree to take part in projects without having to seek permission from the whole group ('closed projects'); there is no automatic *juste retour*, as work-share and/or cost-share are to be decided on a case-by-case basis; participants in a project can choose who is to let

22. During their twentieth meeting on 20/21 March 2003, WEAG NADs themselves accepted the necessity to reconsider the future of WEAG and WEAO, and decided to prepare the ground for a possible transfer of competence to the EU.

23. These rules cover the usual necessary subjects in the area of R&T cooperation, such as contracting, finance, security and intellectual property rights.

contracts for them, and there is no need to submit outline descriptions of projects to WEAG Panel II for approval. Since these provisions meet the expectations in particular of the main arms-producing countries, MOU EUROPA and ERG No. 1 will certainly become the main instruments for the management of future European R&T projects.²⁴

OCCAR

In November 1996, France, Germany, Italy and the United Kingdom signed an MOU on the creation of the Organisation for Joint Armaments Cooperation, OCCAR. Since there was no agreement to establish OCCAR as a subsidiary body of WEU or to include it in the EU, the organisation attained its legal status only after the ratification of its convention, a process that took more than two years (from the signing of the OCCAR Convention in September 1998 until its ratification in Italy in December 2000).

Like WEAO, legally OCCAR has the potential to become a fully-fledged armaments agency. According to Article 8 of the Convention, OCCAR could cover a whole range of activities.²⁵ However, up until now, OCCAR has been purely a management agency, aiming at greater efficiency in the management of collaborative defence equipment programmes. To achieve this objective, its working methods and procedures are based on a number of innovative principles, in particular transnational project teams, simplified approval processes and a more flexible calculation of industrial *juste retour*, replacing the strict application of 'cost-share equals work-share' on a project-by-project basis by a multi-year/multi-programme balance.

OCCAR's main decision-making body is the Board of Supervisors (BoS). According to the OCCAR convention, the BoS consists of the ministers of defence or their delegates. De facto, however, it normally meets (2 or 3 times a year) at a level below NADs. The BoS has delegated some of its functions to other committees (Future Tasks and Policy, Finance, Security and Programme Committees). The Executive Administration (EA) consists of the central office (undertaking corporate processes such as support and human resources, development of new management tools and acquisition of new programmes) and various programme divisions (doing the core business such as programme management, systems specifications, contracts and finance).

24. The first Technical Arrangement (TA) setting up a cooperative project under ERG No. 1 was signed by Italy and the United Kingdom in March 2002. Both the EUROPA MOU and ERG No. 1 are reproduced in Burkard Schmitt, op. cit. in note 1, pp. 95-125.

25. Article 8 of the OCCAR Convention stipulates that it 'shall fulfil the following tasks and such other functions that the Member States may assign to it: a) management of current and future cooperative programmes, which may include configuration control and in-service support, as well as research activities; b) the management of those national programmes of Member States that are assigned to it; c) preparation of technical specifications for the development and procurement of jointly defined equipment; d) coordination of planning and joint research activities as well as, in cooperation with appropriate military staffs, studies of technical solutions to meet future operational requirements; e) coordination of national decisions concerning the common industrial base and common technologies; f) coordination of both capital investments and the use of test facilities.' Quoted in Burkard Schmitt, *ibid.*, p. 47.

Until 2000, OCCAR was mainly occupied with the definition of its own rules and procedures. Several long-standing Franco-German projects like HOT, *Roland* and *Milan* served as pilot projects for framing the new regulatory framework. Now that OCCAR has become fully operational, its main challenge is to demonstrate effectiveness and efficiency in its core business, i.e. the management of cooperative projects. Its most important programmes today are the *Tiger* attack helicopter (FR/GE), the Future Surface-to-Air missile Family (FSAF) (FR/IT) and the A400M transport aircraft (B/E/FR/GE/T/UK). Including the A400M, in 2003 OCCAR's 200 staff are managing a budget estimated at €1 billion. The A400M is of particular importance for OCCAR, not only because of its sheer size but also because it is a test case for the involvement of non-OCCAR members.

So far, member states have decided almost spontaneously and without clearly defined criteria which programmes should be managed by OCCAR. This 'method' is understandable, since there is no European body upstream of the procurement cycle that could prepare the ground for OCCAR in a more systematic way. However, it is a particularly unsatisfying practice, because OCCAR needs more new projects if it is to exploit its potential fully. In fact, all previous and current OCCAR projects have been organised under traditional intergovernmental agreements. Consequently, the work-share has already been defined and (at least prime) contractors selected. Even on these programmes, management by OCCAR helps to reduce overhead costs, but to apply its own principles fully and work on the basis of global *juste retour*, OCCAR would need several new programmes to start almost in parallel.²⁶

OCCAR is open to other European countries, subject to their actual involvement in a substantive collaborative programme managed by OCCAR and acceptance of OCCAR's principles, regulations and procedures. Thanks to its participation in the A400M programme, in late May 2003 Belgium became the fifth OCCAR member, and holds five voting rights in the BoS (as compared with 10 voting rights for each of the founding members).²⁷ Spain, which also participates in the A400M programme, is another candidate for OCCAR membership. However, existing member states refuse to accept the Spanish demand for eight voting rights in the BoS unless Madrid joins another major European project (*Tiger*). Following domestic problems, the Netherlands has

26. See Joachim Rohde and Markus Frenzel, 'Transatlantic Gaps and European Armaments Cooperation', op. cit. in note 3, p. 92.

27. OCCAR's BoS adopts important decisions (admission of new member states, rules and regulations, organisation of OCCAR EA and appointment of the Director) by reinforced qualified majority. This means that a decision cannot be taken if there are ten opposing voting rights. Since the voting rights of founding members are equal to 10, each of them has a veto right de facto. See OCCAR Convention, Annex IV, in Burkard Schmitt, op. cit. in note 1, p. 59.

withdrawn its candidature; Sweden has expressed serious interest but lacks a programme that could open the door to OCCAR.

LoI Framework Agreement

In July 1998, defence ministers of the six major arms-producing countries in Europe signed a Letter of Intent (LoI), aimed at facilitating cross-border restructuring of defence industries. The ensuing consultation process among the participants led, in July 2000, to the signing of the so-called Framework Agreement, a legally binding international treaty covering six areas: security of supply, export procedures, security of information, research and technology, treatment of technical information and harmonisation of military requirements.²⁸ In five out of these six areas, Implementing Arrangements were then drafted to specify in detail how the system should work.²⁹

- In the area of security of supply, participants accept the fact that transnational restructuring implies possible abandonment of national industrial capabilities and mutual dependence. To deal with these challenges, they undertake not to hinder the supply of defence articles and services produced on their territory to the other LoI partners, and to provide them eventually from their own stocks. Moreover, LoI governments will establish an information exchange system on industrial restructuring. This system will be based on national codes of practice with industry: companies signing the code undertake to consult their respective governments before any change of ownership or scope of activity. These governments should then inform all LoI partners who have been customers of the company concerned during the previous three years. Moreover, industry is supposed to sign national codes of conduct containing commitments to accept national priority and reallocation systems for production in the event of a crisis. The Implementing Arrangement lays down common principles for these priority systems, but each LoI country is free to specify the modalities.
- For exports, the main innovation of the Framework Agreement is the Global Project Licence (GPL), aimed at streamlining export procedures for cooperative programmes. If a GPL is granted for a given programme, be it industrial or governmental, the system itself, its subsystems and components can move freely within the territory of the six partners. As for exports to

28. Reproduced in *ibid.*, pp. 68-94.

29. Security of Information is the only area where there is no Implementing Arrangement, because the provisions of the Framework Agreement are sufficiently detailed.

non-LoI countries, states involved in the programme determine by consensus so-called permitted export destinations. The latter are established following industrial proposals and are modifiable in case of significant changes in the political situation in an export destination.

- In the area of security of information, the LoI partners have agreed on general provisions that should be incorporated in future MOUs to be signed on international programmes. They have worked out common principles, requirements and procedures for visits to industrial facilities and government establishments, as well as for the transmission of classified information. Last but not least, they have developed a common understanding of how to deal with national security clearance and agreed on a consultation process in cases where non-LoI nationals need access to classified information.
- In the field of military research and technology, the LoI partners have agreed on the creation of a system for exchange of information, covering R&T strategies and policies, as well as current and planned defence-related R&T programmes. Moreover, they have decided to develop a code of conduct to coordinate their relationships with transnational defence companies. A Group of Research Directors has been set up for this kind of 'top-down' management of R&T cooperation. As for the running of specific projects, the partners have agreed to make use of the EUROPA MOU and ERG No. 1 as the preferred instruments.
- As for the treatment of technical information, provisions of the Framework Agreement aim at developing common standards for dealing with Intellectual Property Rights (IPRs). Since European countries have different rules for ownership of technical information (company-owned or state-owned), IPRs can pose a problem for the creation of a transnational defence company. According to the Implementing Arrangement, the ownership of IPRs should in general be held by companies, with governments keeping some prerogatives in particular on transfers of IPRs and the payment of royalties.
- Regarding the harmonisation of military requirements, the LoI nations have established a new methodology, based on the commitment to inform each other fully about their respective national planning: the six partners have agreed to set up a master data base with a complete list of their future capability

needs. A common board will then try to identify common needs and possible common solutions to those needs. If there is agreement, a cooperative requirement team will be set up to define a common staff target.

It was only in July 2003 that the last LoI country – Italy – ratified the Framework Agreement, and Implementing Arrangements will not be signed before the end of 2003.³⁰ Only then will the Framework Agreement be fully operational. It is therefore too early to say today how the LoI system will work in practice.

It is certain, however, that the LoI process will not lead to a permanent institutional structure. The Executive Committee, which meets four times a year at a level well below National Armaments Directors (except Sweden, whose NAD does attend), will be maintained (a) to monitor the implementation of the Framework Agreement by national authorities and (b) to develop the system further. The possibility of a ‘phase 2’ of the LoI process is under consideration but no decision has been taken yet. In the meantime, the subcommittees on security of supply and treatment of technical information are continuing to discuss certain specific items.³¹ Those for R&T and harmonisation of military requirements are replaced by new mechanisms, and the one on export procedures will probably continue to meet regularly to monitor the actual use of GPLs.

Since its beginning, the LoI process has been caught between pressure to produce concrete results rapidly and a reluctance to engage in more thorough reform. Consequently, its approach has been rather limited, trying to make national rules and procedures compatible with each other rather than setting up a new regulatory framework. Rules and procedures have not been standardised, nor policies harmonised. This self-imposed limitation has led to solutions that are often too complex, vague or not sufficiently binding.

Moreover, the LoI process has evolved under the authority of Ministries of Defence (MOD); other relevant ministries have been involved only through national staffing. This approach is too narrow to cover all the necessary technological, financial and economic aspects of strategic industries. A comprehensive solution would have to embrace trade, industrial, internal market and competition issues that come at least in part under the authority of European community policies.

30. Signing the various documents is a time-consuming process, because each of the five Implementing Arrangements has been translated into the six LoI languages, and each of these 30 documents has now to be signed by all six LoI partners. Moreover, each Implementing Arrangement is signed by a different national authority (National Armaments Directors, Research Directors, export control authorities, etc.). Finally, all documents will be deposited in the United Kingdom as the depository country of the Framework Agreement.

31. The Sub-Committee on Security of Supply is currently discussing offset waivers and their impact on market access; the Sub-Committee on Treatment of Technical Information is working on the harmonisation of contractual terms and conditions, and a specific ad hoc Working Group has been set up to consider export promotion measures.

Finally, the intergovernmental method has proven to be extremely time-consuming and cumbersome. The fact that it will have taken more than three years to accomplish the ratification process and make the Framework Agreement operational is a case in point. Lacking high-level political supervision, technical discussions have dragged on at the working level. These problems may well continue even when the system is operational: some provisions leave plenty of room for interpretation, while others need strong political will to make the agreed mechanisms work. In the absence of continued high-level political input and monitoring, it remains doubtful whether national defence and procurement bureaucracies will be able to put life into the Framework Agreement's provisions.

All this does not mean that the LoI process is a failure. On the contrary, the learning effects alone will be highly beneficial in taking things forward. However, the Framework Agreement and its various Implementing Arrangements can only be the beginning of the process. They do not set up a defence equipment market, but they will serve as benchmarks for more comprehensive solutions. The LoI system needs to be developed, and the method in particular needs to be improved: intergovernmental rule-setting has clearly shown its limits, and the mechanisms set up for cooperation on R&T and harmonisation of military requirements might be too weak to produce the necessary results. Moreover, coordination with other European bodies and political supervision will be indispensable.

Within the EU framework

All the above-mentioned initiatives have been taken outside the EU framework. As we have seen, member states have deliberately excluded armaments from the European integration process, referring to Art. 296 TEC. In its role as regulator of the single market, the European Commission has repeatedly expressed a desire to become more closely involved with European armaments matters. Since 1996, it has launched several Communications on defence-related industries. The second Communication, published in November 1997, called for the creation of an integrated European defence market, based on a proposed CFSP Common

Position and an Action Plan, using a combination of legislative and non-legislative instruments under the first and second pillars.³² However, this initiative has not led to any substantial progress: the draft Common Position has not been adopted by the Council, since member states have disagreed on both the substance and the desirability of a common armaments policy. The Action Plan has been dormant since 1999, and only in the areas of customs duties and standardisation has some progress been achieved.³³

However, in spite of the reluctance of many member states, there are certain armaments-related issues where the EU has developed at least a limited competence.

The dual-use regime

The question of export controls on dual-use goods was first raised in the context of the completion of the European internal market (1992). In order to allow dual-use goods to move as freely between member states as they do within each of them, the EU Council established, on 19 December 1994, a common control regime for dual-use exports to third countries. Based on a Council Regulation and a Council Decision,³⁴ the regime was a cross-pillar approach aimed at coping with the responsibility dilemma concerning the specificity of dual-use goods. As part of trade policy, restrictions on exports of dual-use goods fall within the competence of the Community by virtue of Article 133 (formerly 113) TEC. Therefore, control procedures and mechanisms were outlined in Regulation (EC) 3381/94, which became part of Community law. Council Decision 94/942/CFSP, in contrast, was adopted under Article J.3 of the Maastricht Treaty (now Article 14 of the TEU) concerning joint action in matters covered by the CFSP. Both texts were closely entwined by numerous cross-references and formed an 'integrated system'. The Community Regulation outlined how the regime would work, whereas all lists of permitted destinations and controlled items were annexed to the Council Decision under CFSP rules. Whereas the Commission was charged with the procedural aspects of the system, it was the Council's (and therefore the member states') responsibility to establish, monitor and update the lists. Since the latter are obviously the heart of the control regime, the Regulation alone would have had no substance and

32. 'Implementing European strategy on defence-related industries', European Commission Com (97) 583, Brussels 12.11.1997. Available at: http://europa.eu.int/comm/enterprise/defence/defence_docs/def_comm.htm

33. As for standardisation, the Commission has launched a European 'Defence Standardisation Handbook', containing references to standards and commonly used terms to support defence procurement contracts as well as guidelines on the optimum selection of such standards. The Handbook has been developed with the assistance of the European Committee for standardization (CEN) and participation of MODs and industry. It should be ready in its initial form by the end of 2003 and in a first operational version around the end of 2004. As for customs duties, a council regulation on the basis of Art. 26 TEC was adopted in January 2003 suspending import duties on certain weapons and military equipment. See Council Regulation (EC) 150/2003, published in the *Official Journal of the European Communities*, L25, 20 January 2003, p. 1.

34. Council Regulation (EC) 3381/94 and Council Decision 94/942/CFSP, published in the *Official Journal of the European Communities*, L 367, 31 December 1994, pp. 1-7 and 8-163.

made no sense. The member states' prerogatives were based on the assumption that all decisions concerning the lists were strategic and/or political in nature and, therefore, outside the Commission's competence.

For legal and practical reasons, the integrated system was replaced in July 2000 by a new control regime³⁵ based solely on Article 133. The new Council Regulation (EC) 1334/2000 includes all annexes and is effective without any cross-references to the corresponding Council Decision 2000/402/CFSP. This means that both principles and lists come under the Commission's competence. The Commission now has the exclusive right of initiative, and all Council decisions are taken by qualified majority (instead of unanimity). However, since the list of controlled items is a compilation of lists defined by international non-proliferation regimes (Wassenaar, MTCR, Nuclear Suppliers' Group) where member states – and not the Commission – are represented, the former have preserved a dominant position.³⁶

Apart from that, the updated regime has established a new consultation mechanism on undercutting that will certainly improve cooperation between EU countries. Under the previous regime, a member state could easily grant an export licence for an item for which the authorities of another member state had refused authorisation. Under the new Regulation, such undercutting can provoke considerable peer pressure. Member states now have to (a) inform each other on denials of export licenses; (b) consult with each other on their intention to undercut; and (c) explain their decision to do so. This provision is a (highly) upgraded version of the consultation mechanism of the Code of Conduct for arms transfers (see below). It remains to be seen whether the new consultation mechanism can compensate for the main problem of the control regime – the absence of a common export policy. Today, the regime constitutes nothing more than a common framework for different national policies. Member states recognise each other's export licences but they do not necessarily agree with each other's export policies. Moreover, the common guidelines remain so vague that there is a risk of inconsistent interpretation and application of the provisions by national authorities.³⁷

35. Council Regulation (EC) 1334/2000 and Council Decision 2000/402/CFSP, published in the *Official Journal of the European Communities*, L 159, 30 June 2000, pp. 1-218. Since then, five amendments to the Regulation have been endorsed by the Council (in December 2000, twice in March 2001, in May 2002 and in February 2003). The latest change of the Regulation (149/2003) was published in the *Official Journal of the EU* number L 30. Regulation 149/2003 contains all the consolidated changes made in Annexes I, II and IV since adoption of the Regulation.

36. Burkard Schmitt, 'A common European export policy for defence and dual-use items?', *Occasional Paper 25* (Paris: Institute for Security Studies of WEU, May 2001), pp. 8-9.

37. At the Community level, a coordinating group, composed by national licensing officials and customs officers and chaired by the Commission, regularly discusses the practical application of the regulation. The group focuses on resolving practical problems and developing common interpretations of certain provisions of the Regulation.

POLARM

Within the EU Council, the ad hoc European Armaments Policy Council Working Group (POLARM) is the only formal forum for discussion on armaments. POLARM was set up in 1995 and works directly to the Committee of Permanent Representatives (COREPER). It is made up of foreign ministry representatives, usually accompanied by experts from MODs. POLARM is supposed to meet three times during any one presidency, but its actual activity depends very much on the particular interest of each presidency.

Its initial mandate was (a) to analyse the report of an informal EU/WEU-WEAG group of experts which in 1994-95 studied the options of a European armaments policy, (b) to identify the points in the report which merit further examination, (c) to make recommendations for further action within the EU and (d) to put forward, as appropriate, a list of specific measures without prejudice to the Commission's competence under the TEU. On this basis, the Group has examined many different topics related to EDITB and EDEM, but its overall results have been meagre due to a lack of interest and consensus among member states.

Under the Greek Presidency (January-June 2003), POLARM developed a new dynamic. Within a few months, the group agreed on three draft resolutions that have been adopted by the Council on (a) standardisation, (b) restructuring challenges in the EU armaments sector and (c) security of supply. This was the first time since its creation that POLARM was able to reach agreement on such draft documents. The resolutions contain no concrete commitments and lack substance, but the very fact that they were adopted illustrates a greater willingness to deal with armaments within the EU.³⁸

Under the Greek Presidency, POLARM also started to discuss a 'EU Cooperation Programme for Advanced Research and Technology' (E.P.A.SE.RE.TE). However, following its Communication of 11 March 2003, the Commission has been charged with including the long-term research part of E.P.A.SE.RE.TE in its own preparatory action.³⁹ POLARM, in turn, is supposed to continue discussions on military research.

The Code of Conduct

The European Union Code of Conduct on Arms Exports was adopted on 8 June 1998 by the General Affairs Council as a Council

38. POLARM also drafted a Common Position on intra-Community transfers, which has not been adopted yet. The Commission in particular considers transfers as a first-pillar issue and would therefore prefer an EC regulation rather than a CFSP instrument. However, the text may be adopted under the Italian presidency (second half of 2003).

39. E.P.A.SE.RE.TE contains proposals for rules governing strategic R&T activities that are very similar to those of the EUROPA MOU. The Commission, in turn, has accepted them for the management of its preparatory action.

Declaration in the framework of the CFSP.⁴⁰ The Code of Conduct is a politically but not legally binding instrument, and does not involve the European Commission (normally in charge of trade issues). The overall objective of the Code is to achieve greater transparency in arms transactions and to lead to a growing convergence of national export policies. To achieve this objective, it sets eight criteria that serve as minimum standards for the management and control of conventional arms exports by member states to third countries.⁴¹ Moreover, it establishes an information exchange and consultation mechanism between EU member states. In 2001, a common list of military goods subject to the Code was agreed to serve as a guideline; member states are, however, free to use their own lists.

The first part of the code contains guidelines that set out a number of circumstances in which licences should be refused; the second part gives operative provisions that contain a mechanism for consultation on undercutting and an annual review process.

Consultations on the Code's implementation and operation take place in COARM, the Council's Working Group on arms exports. COARM was set up as an ad hoc group when the Maastricht Treaty entered into force. It is made up of foreign ministry representatives from member states, usually accompanied by defence ministry experts. The group is answerable to COREPER and meets six times a year.⁴² So far, COARM has submitted four annual reports to the Council.

The Code of Conduct has been 'both welcomed as an important step towards a common European approach to arms exports and criticised for its numerous loopholes and shortcomings'.⁴³ It is often criticised for being politically, but not legally, binding which leaves its actual application to the sole discretion of its members. Moreover, vague formulations and compromises based on the lowest common denominator leave plenty of room to interpret the Code according to member states' interests. Beyond that, the Code's consultation obligations have been considered as too weak. If one EU country wants to take up a licence that has been denied by another, it needs to notify and consult only with the member state that first issued the denial. Many EU governments would have liked to see, as a minimum, multilateral notifications of an intention to undercut in order to increase peer pressure and move more rapidly towards a common approach.⁴⁴

40. 'European Union Code of Conduct on Arms Exports', adopted on 8 June 1998. Reproduced in Burkard Schmitt, *op. cit.* in note 1, pp. 29-44.

41. The Code's eight export criteria are based on those defined by the European Councils in Luxembourg (29 June 1991) and Lisbon (26-27 June 1992). These include: (1) Respect for the international commitments of EU members, in particular the sanctions decreed by the UN, the EC, and non-proliferation agreements; (2) The respect of human rights in the country of final destination; (3) The internal situation in the country of final destination, as a function of the existence of tensions or armed conflicts; (4) Preservation of regional peace, security and stability; (5) The national security of the member states, as well as that of friendly and allied countries; (6) The behaviour of the buyer country with regard to the international community, as regards in particular to its attitude to terrorism, the nature of its alliances, and respect for international law; (7) The existence of a risk that the equipment will be diverted within the buyer country or re-exported under undesirable conditions; (8) The compatibility of the arms exports with the technical and economic capacity of the recipient country. *Ibid.*

42. See <http://projects.sipri.se/expcon/euframe/coarm.htm#anchor1193390>.

43. See Burkard Schmitt, *op. cit.* in note 36, p. 12.

44. *Ibid.*, p. 13. Beyond that, the Code is criticised for not tackling all the relevant problems. Licensing of production abroad, for example, has not been addressed. Nor are constraints on the activities of international arms brokering agents included. Several member states have controls on brokering, others not. See <http://www.fas.org/asmp/campaigns/code/EUcodereport4.pdf>.

Nevertheless, in spite of all its shortcomings, the Code of Conduct represents the most comprehensive agreement to date in terms of multilateral efforts to specify how human rights, regional security and development concerns should be addressed within the export licensing process. Regular consultation, joint assessment and progressive work on common definitions help to foster a common understanding of the agreed principles. The more consultation extends beyond specific cases of undercutting and into broader political issues (like the assessment of specific regions), the better the chances of reaching a common export doctrine. However, this will depend mainly on the broader movement towards a true CFSP.

45. See www.europa.eu.int/comm/research/fp6/index_en.html.

46. For more details on these priorities and their respective budget allocations see Decision No. 1513/2002/EC of the European Parliament and of the Council of 27 June 2002, published in the *Official Journal* on 29 August 2002. http://europa.eu.int/eurlex/pri/en/oj/dat/2002/l_232/l_23220020829en00010033.pdf.

47. According to the Commission, objectives of the Community aeronautical research and development activities are to: (a) increase the competitiveness of the European industry with regard to civil aircraft, engines and equipment; (b) reduce the environmental impact of aviation, by reducing fuel consumption, CO₂, NO_x and other chemical pollutants and noise pollution; (c) increase aircraft safety in the context of the substantial rise in air traffic; (d) increase the capacity and safety of the air transport system, in support of a 'Single European Sky' (air traffic control and management systems). Community space activities address: (a) research on satellite-based information systems and services relevant for the Galileo satellite navigation project; (b) research on satellite-based systems relevant for the global monitoring for environment and security (GMES) platform, taking into account the needs of users; (c) advanced research needed to integrate the space and Earth segments in the field of communications. See work programme 2002-06, Thematic priority 1.4., 'Aeronautics and Space', <http://www.cordis.lu/fp6/aerospace.htm>.

EU Research Framework Programme

The Framework Programme is the EU's main instrument for civil research funding. Programmes are proposed by the European Commission and adopted by the Council and the European Parliament following a co-decision procedure. The Framework Programme typically covers a period of four years and has been implemented since 1984. The Sixth Framework Programme (FP6) was decided at the European summit in Lisbon in March 2000 and has been operational since September 2002. Its objective is to establish the 'European Research Area', i.e. an internal market for science and technology. Compared with its predecessors, FP6 has been re-defined and streamlined. Designed to create 'Networks of Excellence' and 'Integrated Projects', it concentrates on fewer priorities and promotes research activities that have a lasting, 'structuring' impact.⁴⁵

Through the Framework Programme, the EU has become an important sponsor of strategic industries. Overall Community participation in FP6 is €17,500 million, which represents 5.4 per cent of all public (non-military) research spending in Europe. For aeronautics and space, one out of seven thematic priority areas of FP6, €1,075 million are allocated.⁴⁶ The aim of activities carried out in this area is to strengthen the scientific and technological bases of the European Aerospace industry, by channelling its research efforts towards priority themes.

The Framework Programme funds only civilian projects.⁴⁷ However, many aerospace companies have both civil and defence activities, and public R&D funding that helps them to remain

competitive in civil markets is all the more important for them, as defence budgets continue to be flat. Moreover, dual-use technologies have gradually been included in the Framework Programmes. GMES, secure telecommunication and safety of IT networks, for example, are all civil but security-related research programmes. They might well lead to applications that are of military interest, in particular in the IT and electronics sector, where military components and systems are increasingly developed on the basis of civil technologies.

At the declaratory level, the link between military and civil research and the need to adapt the EU's research activities accordingly are increasingly accepted. In its Presidency Conclusion of 20-21 March 2003, for example, the European Council explicitly recognised 'the role that defence and security related R&D could play in promoting leading-edge technologies and thereby stimulate innovation and competitiveness', and invited 'the Council to analyse the role of defence R&D procurement in the context of the overall R&D activities in the Union, including the possible creation by the Council of an inter-governmental defence capabilities development and acquisition agency.'⁴⁸ E.P.A.SE.RE.TE and the Commission's preparatory action point in the same direction.

ECAP

At the Helsinki European Council in December 1999, EU Member States set themselves the headline goal of being able, by 2003, to deploy within 60 days and sustain for at least one year forces up to corps level (60,000 men). One year later, at the Capabilities Commitment Conference in Brussels, they committed themselves, on a voluntary basis, to making national contributions to these EU rapid reaction capabilities. The comparative analysis of both the 'Helsinki Headline Goal Catalogue' (specifying the operational requirements for the Petersberg Tasks) and the 'Force Catalogue' (setting out national commitments) revealed considerable shortfalls in national capability commitments. Among the 38 capability shortfalls identified in the so-called 'Helsinki Progress Catalogue', 21 were evaluated as 'significant'.

At the Laeken European summit in December 2001, the EU Council decided to launch the 'European Capabilities Action Plan' (ECAP) to address these shortfalls. From March 2002 onwards, 19 panels of national experts developed possible

48. See Presidency Conclusion of the Brussels European Council of 20/21 March 2003, available at: <http://ue.eu.int/newsroom/makeFrame.asp?MAX=&BID=76&DID=75136&LANG=1&File=/pressData/en/ec/75136.pdf&Picture=0>.

solutions. These panels met independently and were composed of at least one lead nation per panel, active participants and observers. The work of the panels was coordinated by the 'Headline Goal Task Force', which drew upon the support of the EU military staff (EUMS). Panels presented their final report 1 March 2003.

The shortfalls identified vary widely in importance, nature, operational implications and the possible ways to rectify them. One category can be addressed if member states revise their contributions and offer capabilities they already have but which, for various reasons, have not been put forward before.

A second category, however, consists of shortfalls for which capabilities do not exist in national inventories and which can only be rectified if member states acquire the required capability. Some of these shortfalls can be temporarily addressed by short-term solutions such as leasing or upgrading. For a number of shortfalls, including some related to strategic capabilities, a long-term solution would require large-scale procurement projects. Some of these projects are already under way, others not.

During the first phase, neither national planners nor procurement specialists were involved in the panel's work, leaving somewhat unclear if and how ECAP would actually lead to the development of the required new capabilities. However, following an evaluation by the EUMC, at the Capability Conference on 19 May 2003 member states established ten project groups 'focused on the implementation of concrete projects, including solutions through acquisition or other solutions such as leasing, multinationalisation and considering possibilities for role specialisation'.⁴⁹

ECAP is generally considered a promising approach for tackling capability shortfalls.⁵⁰ It has, however, several weak points: first, it remains voluntary and lacks credibility as long as commitments are not underpinned with the necessary funding. Second, ECAP lacks leadership. Member states are free to participate and to take on commitments, and the EUMS apparently has had difficulties to follow, let alone coordinate, the work of the various panels. Last but not least, ECAP remains a purely ad hoc exercise, limited both in time (focusing only on current shortfalls) and scope (dealing only with shortfalls in commitments to the Headline Goal Force).

49. See Council of the European Union, 'Declaration on EU military capabilities', 19 May 2003, p. 4. The 10 project groups are: air-to-air refuelling, combat search and rescue, headquarters, NBC protection, special operations forces, theatre ballistic missile defence, unmanned aerial vehicles, strategic airlift, space-based assets, interoperability issues and working procedures for evacuation and humanitarian operations.

50. See General Affairs and External Relations Council, meeting of defence ministers, Brussels, 19 November 2002, reproduced in Jean-Yves Haine, 'From Laeken to Copenhagen. European defence: core documents', *Chaillot Paper 57* (Paris: EU Institute for Security Studies, February 2003), pp. 147-55.

All these initiatives, institutions and policies have developed without coordination. Membership partly overlaps, but there are neither institutional linkages nor a common strategy. The various areas of armaments are not systematically covered and important gaps persist.

- WEAG, and in particular Panel II, has developed certain methodologies and legal instruments that will be useful for future arrangements. In general, however, WEAG's relative failure shows that the traditional intergovernmental method cannot cope with today's challenges. Even in R&T, cooperation has suffered from a lack of support from member states, and, more precisely, from the Research Cell's limited staff and restricted mandate (to administrative and contractual support). A general lesson to be learned from WEAG's experience is therefore that an organisation for armaments cooperation needs sufficient resources, a strong mandate, high-level representation, workable decision-making processes and, if possible, permanent bodies if it is to be efficient. Moreover, commitments on the opening of defence markets will only work if they are legally binding.
- OCCAR is potentially a very useful tool, but it lacks new programmes to fully apply its own principles. Moreover, it needs greater autonomy vis-à-vis member states. Political guidance is indispensable, but OCCAR should not be kept on a leash by national procurement agencies, which consider OCCAR also as a potential rival.
- The LoI Framework Agreement is only an intermediate step on the way towards a homogeneous defence economic space. In the end, only a supranational body will be able to counterbalance national egoisms and establish a single set of rules. Another general lesson to be learned from the LoI process is that close and permanent political supervision is needed to

ensure that reforms do not get stuck at the working level. Last but not least, the mechanisms that are foreseen for harmonisation of military requirements and R&T are hardly innovative. It is difficult to see why they should perform better than other traditional intergovernmental forums have done in the past.

- The dual-use regime as such is not relevant to this paper, but its underlying philosophy, i.e. free intra-community circulation of items based on mutual recognition of export decisions to third countries, could inspire future arms transfer and export arrangements. As for the Code of Conduct, its consultation mechanisms could certainly be improved, but a common export policy is still a long way off. However, more efficient export procedures should be envisaged in particular for cooperative projects.
- POLARM has a modest record. As a typical intergovernmental body, it depends completely on the political will of national governments. As a result, it has been paralysed for many years by the traditional divergences between member states on armaments. However, its importance might increase in the future, in particular as a forum for discussion between member states and the Commission on the various Communication initiatives.
- The EU Framework Programme is a very positive instrument for fostering research and support strategic industries. It already covers some dual-use activities, but security-related research should be explicitly included. This means, in turn, that there must be a coordinated strategy between the Commission and the future Agency.
- The ECAP process has been an important first step towards a common attempt to tackle capability needs. However, its scope is too limited and its working methods (regular meetings of national experts) follow the traditional intergovernmental patterns. The process should be strengthened, institutionalised, based on permanent groups and linked to procurement and research.

The challenge now is to use the existing useful elements, improve and complement them, and integrate them into a coherent structure. The problem is, again, the complexity of the armaments sector. The creation of an Agency is mainly an institutional challenge, whereas the establishment of a defence equipment market involves

framing new regulations and represents most of all a juridical task. Moreover, the role of the various actors is different. The Commission will play a major role in the development of a defence equipment market, whereas the creation of the Agency will be an exclusive decision by member states (even though the Commission will have an indirect role in defining the Agency's research activities).

The multitude of actors involved does not make it any easier to establish a coherent framework. Within each member state, various administrative branches are in charge of armaments, but these often have difficulties reaching common national positions. These difficulties multiplied by 25 amount to a serious risk that too many cooks may spoil the broth. On top of that, several formal and informal bodies are involved at the EU level (COREPER, PSC, POLARM, several Commission DGs, EUMC, Informal Advisory Group of EU defence ministers, EU NADs, etc.), which almost inevitably implies inter-institutional rivalry and frictions.

As for market issues, the various initiatives announced by the Commission will set the agenda for discussions that will certainly take several years. The work of the Agency, in contrast, will now rapidly become substantial. The Presidency Conclusions of Thessaloniki set a clear deadline that will drive the process – even if the deadline is in contradiction with the schedule for the new EU Treaty. End of July 2003, COREPER agreed on the necessity to establish an ad hoc working group to implement the Presidency Conclusions and to lay the groundwork for the Agency. Whether this group will be able to ensure that the project does not (again) become a victim of national egoism and bureaucratic inertia remains to be seen. However, the fact that COREPER will be in charge of ensuring the coherence of the project is a positive sign, because it takes into account the cross-pillar nature of many armaments-related issues.

There are of course different models for such an Agency: it could be a small central office coordinating existing bodies, a loose network of different agencies, or its scope could be limited to filling certain gaps in the procurement cycle. However, the Agency should by no means become 'just' another armaments institution added to the existing ones. Its creation must be an occasion to rearrange the current setting, leading to a coherent workflow throughout the procurement cycle.

The following model suggests how the Agency should – from the author’s point of view – ideally work. Drawing lessons from the failure of WEAG’s work on the EAA, the emphasis is on processes and competencies rather than technical procedures.

The European Armaments, Research and Capabilities Agency (ARCA) – a blueprint

Cooperation in the broader sense of the word will be the core activity of any future European Armaments, Research and Capabilities Agency (ARCA). In this context, its main objective should be twofold: first, it must ensure that the capability needs of Europe’s armed forces are met, wherever possible, through European cooperation in order to foster standardisation of military equipment and generate economies of scale. Second, it must enhance the efficiency of cooperation in order to exploit potential cost savings effectively. To achieve this objective, the ARCA should:

- cover all relevant procurement phases from the definition of capability needs to in-service support;
- ensure in particular the interaction between harmonisation of military requirements and research;
- avoid unnecessary duplication and integrate existing tools if appropriate;
- work closely with other relevant bodies;
- go beyond the traditional intergovernmental method;
- have high-level political supervision and support.

As shown earlier, OCCAR is potentially a useful tool for the management of cooperative programmes. What is missing is a systematic approach towards the harmonisation of capability needs and military research. In consequence, the future ARCA should (a) fill this gap and (b) use OCCAR as its instrument to cover the subsequent phases of the procurement cycle. To do this, the ARCA should have three functional divisions: capabilities, procurement and research. Given the range of its missions, it should also have units for the monitoring of industrial capabilities and the management of European test facilities.

Capabilities

In order to foster armaments cooperation, the ARCA must, first of all, obtain exhaustive information about European force planning from relevant military bodies. As long as there is no central European planning system for all member states, input must come from national and EU military planning staffs. Since capability needs for the EU Rapid Reaction Force are merely a subset of national needs, information on national planning is key in identifying as many occasions for European cooperation as possible. Both the EUMS and national authorities should therefore inform the ARCA regularly and with as much detail as possible about their planning for the future (with the only exception of highly sensitive capabilities for which member states exclude international cooperation).

EU and national needs should be categorised in core capability areas. Both military planners and the ARCA should work with the same set of categories. The latter must be general enough to reconcile diverging doctrinal preferences. The categories defined by the LoI subcommittee on harmonisation of military requirements could be used for this purpose: (1) Command, Control, Communications and Information, (2) Intelligence, Surveillance, Target Acquisition and Reconnaissance, (3) Deployability/Mobility, (4) Effective Engagement, (5) Protection/Survivability, (6) Sustainability/Logistics, (7) General Support.

To be as efficient as possible, the ARCA should have 'Capability Groups' to follow each of these categories. In contrast to the ECAP panels, these 'Capability Groups' should not only work on current shortfalls, but monitor capabilities over a long period (up to 20 years, depending on the capability). Their main task should be to analyse at what moment in time and in which area a new need will arise, and which technological possibilities will exist at that moment to meet the respective shortfalls. Such a, long-term, approach is the only effective way to harmonise replacement schedules and military requirements. If future national shortfalls had an impact on the EU Rapid Reaction Force, the 'Capability Groups' should also evaluate whether the capabilities in question can be provided by other EU nations and, if so, for what period.

These 'Capability Groups' should have a permanent core of

military and procurement experts (the latter could also come from industry), recruited directly by the Director of the ARCA. This permanent staff would organise regular meetings with national experts to get input and advice from member states. In a first step, 'Capability Groups' would act as a clearing-house, verifying and evaluating national planning from a common European perspective. At this stage, the objective would be to avoid as early as possible unnecessary duplication and foster specialisation. In a second stage, the Groups should compare the revised national planning and identify (a) if several member states list the same capability needs, and (b) which capability gaps are not mentioned by any member states.

'Capability Groups' would then report these findings to the Director of the ARCA. To make sure that these findings have an impact, the latter should be able to present them directly to defence ministers (in an annual 'Capabilities' report, for example). Within a given time, ministers would then have to report back to the Director how they intend to deal with the identified shortfalls.

If two or more ministers stated their interest in working together on one of the identified capability gaps, the 'Capability Groups' would start to explore future technological options to meet those needs. To achieve this objective, the 'Capability Groups' would cooperate closely with the Agency's research division and industry. If necessary, they would launch feasibility studies, which should be financed through an autonomous ARCA research budget (see the ARCA research activities below).

Procurement

To ensure continuity, the ARCA should also be in charge of the subsequent phases. If, after the first technological evaluation, two or more member states wished to continue to work on a given shortfall, the ARCA would either launch a capability-related research programme or set up a permanent 'Project Group'. The decision would depend on the time horizon of the capability need and the maturity of the technology available. Capability-related research programmes would aim at deepening the technological know-how in defence-related fields of research, whereas 'Project Groups' would translate defined capability needs into procurement projects.

More precisely, the objective of a 'Project Group' would be to

identify the most cost-efficient technological solution for the identified capability need. The Group would evaluate technological options, identify the required industrial capabilities, make a cost analysis and formulate a staff requirement.

Members of 'Project Groups' should be military and procurement experts, detached (or seconded) from participating nations. However, they should report to the Director of the ARCA and work under his authority. The Director would, in turn, be responsible for progress made in the 'Project Group'. He would help to settle possible disagreements between the experts, if necessary through intervention in national capitals.

Once the most cost-effective solution(s) had been defined, the 'Project Group' would present its findings to the Director of the ARCA, who would then report to the ministers of the participating nations.

However, cost-effectiveness might not always be enough to convince national stakeholders (both institutional and industrial) of the virtues of a common project. Therefore, a mechanism that generates peer pressure should be invented to counterbalance possible resistance from national defence establishments. If the minister of one participating country refuses the solution proposed by the ARCA, he should be obliged to justify his decision vis-à-vis his colleagues from the other participating nations, his head of government and his national minister of finance.

Once ministers of participating nations have agreed on the proposal of the ARCA 'Project Group', the project would be passed over to OCCAR for management of the development and production phases. Contracts would be let according to OCCAR's current principles and rules. OCCAR would manage ARCA projects throughout their life cycle (but could also, as it does today, outsource in-service support and maintenance, if appropriate).

This scheme applies to cooperative projects only. However, the ARCA could also manage national projects, if, for example, a single nation decides, in response to the analysis by the ARCA 'Capability Group', to tackle a specific shortfall. The possibility to give national procurement projects to the ARCA should be of particular interest to smaller and/or new EU member states, who will normally have small investment budgets and few 'big' procurement projects. For them, the ARCA could be a cost-effective alternative to standing procurement agencies. This, in turn, could help to

reduce or avoid duplication of (costly) administrative structures.

This means, however, that the ARCA should also have a mandate for off-the-shelf procurement, in particular for non-producing countries. Harmonisation of capability needs makes sense even if it does not lead to the development of a new project. If several buyer countries pooled their orders via the ARCA, they would multiply their purchasing power and get better value for money. In this case, the ARCA would have to set up special 'Project Groups' whose objective would be to come to an agreement on the system to be acquired.

The ARCA's off-the-shelf function could also cover non-military goods. Armed forces spend millions of euros each year on all sorts of commercial items, ranging from coffee cups and glasses via pencils and paper to chairs, desks, etc. Pooling these purchases at the EU level would increase the negotiation power vis-à-vis suppliers and could generate enormous cost savings through economies of scale.

Research

Military research and technology is probably the most difficult area for cooperation: First, in Europe, very few countries have significant military R&T activities, and national sensitivities are particularly strong in this area. Second, technology is the key to industry's competitiveness; defence companies are therefore reluctant to share their research findings with potential competitors. Third, military R&T is difficult to define. Advanced (or pure) research normally takes a bottom-up approach: it is not driven by a specific demand, and its objective is technological innovation per se. As a result, it is normally too early to say at this stage whether research will lead to a practical application at all, and, if so, whether this application will then be military, commercial or both. Capability-related research, in contrast, follows a top-down approach. It is driven by a more or less clearly defined need of the armed forces and oriented towards a specific end. If, finally, research is already project-related, it can often be considered as 'Phase 0' of the development phase. The logic underpinning these three categories of research is certainly different – in practice, however, the distinction between them is often blurred, which makes it difficult to define responsibilities and sources of funding.⁵¹

Moreover, the future institutional setting in this area is partic-

51. See David Versailles, Valérie Mérimond and Patrice Cardot, *La Recherche et la Technologie, Enjeux de Puissance* (Paris: Economica, 2003).

ularly difficult to foresee since the Commission is currently working on a preparatory action on security and defence-related research ‘to implement some specific aspects that would be particularly useful in carrying out Petersberg Tasks’. The preparatory action should prepare the implementation of the so-called ‘Agenda for advanced research relating to global security’. It should not take longer than three years and is supposed to acquire ‘experience for evaluating the conditions and arrangements needed for effective cooperation between national research programmes’.⁵² One can safely assume that this preparatory action will have an impact on the future organisation of security- and defence-related research in Europe. It also confirms that advanced research should and will become a joint effort by member states and the Commission.

In spite of these uncertainties, the ARCA should have a specific division for military research, mainly because of the link between technology, research, development and acquisition. More specifically, the ARCA’s research division should finance and manage capability-related research up to the level of demonstrators. Product development, in contrast, should stay with OCCAR. Advanced research follows its own logic and should therefore be managed by a separate body (but in coordination with the ARCA and the Commission). Such a division of labour would correspond to the above-mentioned specificities of R&T.⁵³

In comparison with procurement programmes, R&T projects are more numerous, smaller (in financial terms) and very different in nature. R&T activities therefore need to be governed by specific, very flexible rules and procedures. ARCA must therefore at least be allowed to use the MOU EUROPA and ERG No. 1 as legal instruments for its R&T projects.

A close link between R&T and harmonisation of military requirements is essential. There must therefore be permanent and intensive cooperation between the ARCA’s research division and its ‘Capability Groups’. The former would provide technical expertise, evaluate research findings and let contracts on behalf of the latter, both for preliminary studies and (more costly and complex) capability-related research programmes. These programmes, launched as follow-ups to the analysis of ‘Capability Groups’, should have as their goal the creation of demonstrators. The findings of these capability-related research programmes would then serve ‘Capability Groups’ as the basis for further work

52. See Commission Communication, reproduced in op. cit. in note 1, p. 176.

53. Cooperation on advanced research means mainly exchange of information, whereas the work on demonstrators can (already) be divided into more or less independent packages. This makes it easier for companies to ‘control’ the sharing of their research findings and thus facilitates industrial cooperation. Advanced research is more suitable for broad participation and widespread dissemination of findings than project- or capability-related research, because its potential commercial applications are of interest to all member states. Moreover, long-term innovation often comes from small companies and laboratories that are not necessarily located in the Lol countries.

54. At the early stage of the procurement cycle, only small amounts of money are needed for feasibility studies, demonstrators, etc. Having an autonomous budget for these needs would accelerate cooperative projects considerably.

55. Industrial participation in military research funding is a controversial issue that merits further exploration. In the United States, military research is purely government-funded. European governments, in contrast, often demand that their industries participate in research costs in order to share the financial risk. Later on, this research share is then reimbursed as part of the production costs. In practice, this can greatly reduce the flexibility of a programme: The more companies participate financially in research activities, the more they depend on the actual production of the system. At the same time, defence industries are strategic industries, and governments therefore do not want to damage them financially. This can lead to an automatism whereby a certain number of a given weapon system 'has' to be produced to compensate industry for its research investment. In a sector where procurement cycles are extremely long and industrial, technological and military realities evolve (quickly), such a loss of flexibility can entail important financial risks at the later stage of a programme. A possible compromise could be to limit industrial co-funding of research to projects where production is at least probable. This is normally the case for short- to medium-term projects and/or when a project is nearing the industrialisation phase. However, customers like ARCA can only bear the financial risk alone if they have the capacity and the know-how for a precise definition and a thorough evaluation of research projects.

56. François Heisbourg, Jean-François Daguzan, Martin Lundmark and H  l  ne Masson, 'The European Defence Industrial Base and ESDP', in *Prospects on the European Defence Industry* (Athens: Defence Analysis Institute, 2003), p. 57.

on the respective capability shortfall.

All research activities initiated by 'Capability Groups' (preliminary studies and capability-related research programmes) should be financed through an autonomous ARCA research budget.⁵⁴ Ideally, this budget should be co-funded by member states (calculated on a GDP basis), the European Union (CFSP or research budget line) and, possibly, industry.⁵⁵ The idea here is to match every national euro by an EU euro in order to create an incentive to earmark more national R&T funds for the ARCA.⁵⁶

Such a funding mechanism implies that all member states would have access to the research findings. However, this is unlikely to lead to new duplication if the ARCA is free to select the contractors for its research projects. In fact, only a few companies are able to build demonstrators, and IPR arrangements can ensure that most of the generated technological know-how would stay within the company in charge. This implies, in turn, that industries located in LoI countries would probably benefit most from the common funding. This seems politically acceptable: first, it would be an important incentive for LoI countries to let the ARCA manage their R&T programmes rather than set up ad hoc arrangements. Second, such subsidising must be seen in the general context of EU solidarity: non-LoI countries often receive considerable EU subsidies in other areas. Their contribution to a common research fund seems therefore justified even if it does not imply a guaranteed industrial or technological return on investment, in particular since it would be relatively modest (calculated on a GDP basis) and serve a common objective (strengthening ESDP in general, EDITB and military capabilities in particular).

The closer a project comes to the actual procurement phase, the more reluctant member states and industry will be to share findings with non-participating partners. At the same time, the latter will probably refuse to pay for a project in which they are not involved. As a result, research activities of 'Project Groups' should be funded exclusively by participating nations, and the latter should not be obliged to disseminate results. The ARCA research division could nevertheless let research contracts on behalf of 'Project Groups'.

The ARCA's research staff should consist of permanent agents, recruited from the WEAO Research Cell, the European Commission, industry and laboratories. If the Research Cell were transformed into the ARCA's research division, its missions, which are

currently limited to administrative and contractual support to WEAG member states, would have to be redefined (to allow in particular for technical assistance to ARCA ‘Capability Groups’). Instead of incorporating the Research Cell as an organisation into the new structure, it would probably be more advisable only to transfer its personnel.

The ARCA should also have a scientific board, consisting of national research directors and representatives of the Commission. The board should exchange information about R&T strategies, harmonise national R&T plans, and stay in permanent and close dialogue with industry. Moreover, the board would decide by Qualified Majority Vote which studies and capability-related programmes proposed by the ARCA Director should be commonly funded. However, ARCA’s research division and the Director would then be free to select the companies to which research contracts would be awarded. The board would supervise the work of the ARCA research staff, but not intervene in the operational business.

The Group of Research Directors (GRD) established under the LoI Implementing Arrangement should be incorporated into the ARCA’s scientific board. However the GRD must have the right to form subcommittees, operating as ‘closed shops’. Restricted subcommittees can also be established for monitoring the activities of ‘Project Groups’. The board would develop a strategy for the ARCA’s own research activities and coordinate them with those of other relevant bodies.

The ARCA’s scientific board should in particular provide technical expertise to the Commission for the part of the Framework Programme related to security. As to the latter, the Commission should formulate explicit guidelines for evaluators of research proposals, ‘stating formally that the dual-use potential of a project cannot count against it’. Even better would be to define ‘specific horizontal actions . . . to encourage the application to civil goals of technological capabilities developed in military contexts’, and to include in the Framework Programme ‘specific actions funding research in key dual-use technology fields’.⁵⁷

On top of that, it would make sense to complete the ARCA – as the EU’s agency for defence research – by a specific European Strategic Research Agency (ESRA). POLARM has already discussed the creation of such an Agency within the framework of E.P.A.SE.RE.TE, and the Commission’s preparatory action might

57. Jordi Molas-Gallart, ‘Coping with Dual-Use. A Challenge for European Research Policy’, *Journal of Common Market Studies*, vol. 40, no. 1, pp. 155-65, here p. 162.

well come to the same conclusion. Following the American DARPA model, this ESRA should focus on technological innovation at the earliest stages of the research process, where projects inevitably run a high risk of failure. The activities of this ESRA could be driven by military and security considerations, but its missions would explicitly include cross-fertilisation between the military and civil sectors and dual-use applications. Such an ESRA should thus be managed and funded jointly by the Commission and member states.

Monitoring EDITB

There is a close link between military capabilities, research, development and acquisition, on the one hand, and the Defence Industrial and Technology Base on the other. First, industry's technological capabilities determine the options for tackling future military shortfalls and are therefore key factors when taking procurement and research decisions. Second, research and procurement choices shape the EDITB, because it is the customer's investment decision that determines which capabilities industry develops (or abandons). Given the long procurement- and life-cycles of defence systems, this also means that long-term planning for the use of research and production facilities is crucial if the loss of industrial and technological capabilities is to be avoided.

Governments normally have an overview of their national assets, but it would make sense to complement the information defence ministers get from their national services with European expertise. The more 'European' the industry becomes, the more important it will be to get a global picture of the European industrial landscape as a whole. Monitoring the EDITB would therefore be highly desirable.

In its Communication of March 2003, the Commission declared its intention to launch such a monitoring activity, and the Council has adopted a resolution supporting this initiative.⁵⁸ However, this task should probably be attributed to the ARCA. First, ARCA itself needs a sound knowledge of industrial and technological assets to present possible solutions for future capability needs. Second, ARCA can only act as an 'intelligent' customer and manage its research projects efficiently if it has the expertise to define and evaluate projects, which in turn requires knowledge of industrial capabilities. Third, its own core activities – analysis of

58. See *op. cit.* in note 48, para. 35.

military capabilities, financing of defence research and programme management (through OCCAR) – will make it much easier for ARCA than for the Commission to collect information on the EDITB. Last but not least, ARCA will – hopefully – have a direct link to defence ministers and therefore be well placed to help them develop a truly European defence industrial strategy.

For all these reasons, ARCA should dispose of its own unit to monitor the EDITB. This unit should draw on information from ARCA's functional divisions, companies, and the LoI's information exchange system for security of supply. It should follow closely the development of Europe's industrial and technological capabilities, identifying current overcapacities, alerting impending undercapacities and analysing corporate trends (in particular changes in ownership and investments from outside the EU). The unit's finding should be included in the ARCA's annual capability report that the Director presents to ministers. At the same time, the ARCA's monitoring unit should establish a close link with the Commission's relevant DGs (a) to receive data on defence companies' civil activities, and (b) to give information about the restructuring of defence industries (which might have an impact on competition and/or imply accompanying social and regional Community measures). In time, the link between the ARCA and the Commission should be developed into a joint Monitoring Task Force. The more the Commission becomes involved in defence market and research issues, the more it will make sense to develop such a body that would monitor the complete range of aspects of defence economy in support of a truly comprehensive strategy for strategic industries.

Management of test facilities

Test and evaluation form a vital part of the development of military systems, and the major arms-producing countries in particular have built up a broad spectrum of test facilities. There is thus considerable duplication of assets in Europe. If EU members agreed to use facilities jointly this could generate important cost-savings.

As early as 1992 WEAG created a Sub-Group on Test Facilities (SGTF) as a subgroup of Panel II. The SGTF is tasked to analyse the actual use of European test facilities and make recommendations for their better utilisation. It has compiled a directory of test centres in WEAG countries and developed a database of informa-

tion on these facilities. Moreover, all WEAG members have signed an MOU that acts as an umbrella for the reciprocal use of test facilities.⁵⁹ However, there is neither a common strategy for the future nor a concept to reduce existing redundancies across national borders.

ARCA should therefore take over this function from the SGTF and develop a more ambitious approach. It should, first of all, define a strategy for rationalisation, including concrete proposals for reciprocal and joint utilisation of existing facilities, common investments and the coordinated reduction of duplication. Since such a strategy would not be implemented overnight, ARCA should also monitor the actual utilisation of facilities in EU member states and include its findings and recommendations in its annual capability report. At the same time, ARCA should be able to decide autonomously which facilities it wants to use for its own tests and evaluations. ARCA could then use the projects managed by its divisions to influence the utilisation of test capacities and contribute to the rationalisation of this area. In future, test and evaluation facilities should become common assets managed directly by the ARCA.

Requirements for success

In the model suggested, the Director of the ARCA would be in a particularly strong position. He would orchestrate the work of the various actors and take care that the system as a whole worked properly. At the same time, the Director would be in charge of contacts with other relevant bodies, namely the EUMS/EUMC, the EU Council, the Commission and national authorities.

Vis-à-vis member states, he would act as a genuine European advocate of cooperation in general and ARCA projects in particular. This role is particularly important, since the ARCA will have to operate in an intergovernmental environment. Even with a strong mandate and flexible rules, its success will depend on the willingness of member states to give the necessary input and to follow-up to the ARCA's proposals and initiatives.

To achieve this objective, the Director of the ARCA must have direct access to the highest political level. His interlocutors should therefore be defence ministers. They should establish an EU armaments council, acting as the ARCA's supervisory board, to assure high-level political guidance and control. To make the relation-

59. See <http://www.weu.int/weao/site/frameset.htm>. The active use of these instruments varies greatly among WEAG member states. Since its signature in 1998, the MOU has been used 16 times as a basis for bilateral test arrangements, with France far ahead of all other partners (12 times). Information provided for the Directory and Database also differs greatly both in quantitative and qualitative terms.

ship between the ARCA and its supervisory board as fruitful as possible, the Director of the ARCA should also be a politician (rather than a civil servant), ideally a former defence minister who can talk on equal terms with current ministers.

This in turn means that the Director would not be a 'real' expert on armaments. He should therefore be supported by executive directors who have the necessary professional experience in their respective field. Selected by the Director, they would head the functional divisions (capabilities, procurement and research) and be responsible for the operational business.

Many functions contained in this scheme already exist in other forums, and the various services of the ARCA would certainly draw on methodologies previously used by others. However, the model proposed offers some important innovations. The operational strength of this ARCA would be that it could (a) work in a *long-term* perspective, (b) draw on *both* national *and* EU force planning, (c) have *permanent* groups and (d) establish an effective link between planning, procurement and research.

All four elements are key to successfully covering the early phases of the procurement cycle. Building on the experience of the ECAP process and the envisaged LoI mechanisms, this approach would make possible the efficient harmonisation of operational requirements. The ability to draw on an autonomous research budget would enhance the Agency's flexibility and accelerate the launch of common projects. At the same time, permanent common bodies would be in charge right from the beginning, 'protecting' potential cooperative projects during their embryonic phase against national egoisms and bureaucratic inertia, which have often paralysed traditional intergovernmental arrangements.

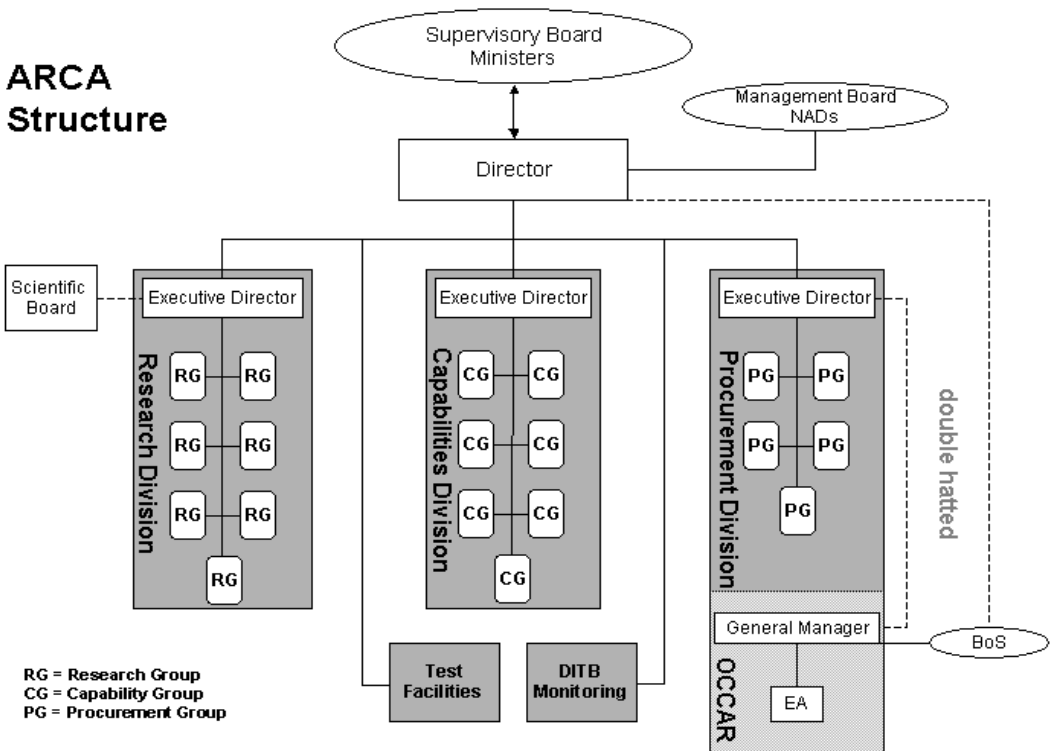
From the development phase onwards, OCCAR would automatically be in charge of all ARCA procurement projects. This automatism should help increase the number of programmes managed by OCCAR. The institutional challenge is to find a link between OCCAR and the ARCA that, on the one hand strengthens OCCAR's role vis-à-vis national governments, and, on the other, preserves its *acquis*. From this point of view, neither full integration (implying that all ARCA countries are members of OCCAR) nor loose association (roughly continuing OCCAR's institutional status quo) seems a realistic option. A reasonable alternative would be to merge only certain functions at the top of the two bodies: the Executive Director for procurement would be double-

hatted, holding also the post of OCCAR General Manager, and the ARCA Director would become chairman of the OCCAR Board of Supervisors.⁶⁰ At the same time the current criteria for membership of OCCAR would be maintained, i.e. it would be open to ARCA member states that participate in a major project managed by OCCAR and accept OCCAR's principles of operation. Those that are not participating in a programme managed by OCCAR would be represented indirectly through the ARCA's supervisory and management boards.

National services would be involved in the work of the ARCA through experts who provide expertise and advice to both 'Capability Groups' and 'Project Groups'. Moreover, NADs could form the ARCA's management board, dealing with the ARCA's administrative issues. However, the ARCA's statutes must make clear that the ARCA is in charge of armaments cooperation and that, for this particular purpose, national administrations are at the service of the ARCA (and not the other way round).

60. A similar structure should be established for research, with the Executive Director for research chairing the ARCA's scientific board.

ARCA Structure



To be efficient and effective, the ARCA will need not only a sound legal basis but also the necessary means and sufficient staff. Such an investment would make sense, since a successful ARCA will achieve greater standardisation and more efficient cooperation, thereby generating additional cost-savings. Moreover, extra personnel costs at the ARCA level can – and should – be compensated by reductions in national procurement agencies. On the other hand, there should be strict controlling mechanisms to ensure that the ARCA itself becomes a model of cost-effectiveness. This controlling should be done by the ARCA itself, but also by independent external consultants.⁶¹

External controlling should also ensure that the ARCA does not become a victim of the classical weaknesses of administrations: over-regulation and excessive bureaucratisation. The OCCAR experience shows clearly that even new and relatively innovative organisations are not immune to these vices.⁶² For the ARCA, they should be avoided at all cost.

In general, the ARCA's working methods should be as commercial as possible. This supposes a high degree of autonomy vis-à-vis member states, both in financial and management terms. Lean structures, flat hierarchies and a maximum of delegation of responsibilities and authority to the actual management level are key. The Director of the ARCA, together with his executive directors, should be responsible for recruitment and dismissals, basing decisions exclusively on competence and performance.

This model is, of course, nothing but a broad outline that needs to be spelt out in detail. Even if a basic structure is set up in 2004, it will certainly take time for ARCA to become fully operational. Existing elements must be brought together and effectively linked, new bodies created, personnel recruited, procedures established, etc. Once it is established, ARCA will again need time to reach cruising speed and even more to make its weight felt. In other words, the establishment of ARCA will be a process spread over a considerable period of time rather than an act at a given moment in time. This process contains many unknowns, in particular since ARCA will evolve in an institutional environment that is itself in transformation. It is therefore particularly important to develop and maintain both an ambition and a vision of what the Agency should become, namely a serious European actor that complements national policies in the most effective way. At the same time, one should never forget that even a powerful ARCA

61. Another possibility would be the creation of a permanent European Controlling Office to check the cost-effectiveness of both the ARCA and national procurement agencies.

62. According to OCCAR staff members, the organisation has developed 35 different management procedures, of which only 5 are actively used in practice.

will not *by itself* be able to solve all the problems of Europe's armaments sector. It will be equally important to overcome progressively the current fragmentation of Europe's defence market.

A common European Defence Equipment Market (EDEM)

The creation of a common defence market is the third element in an effective reform of the European armaments sector (beyond the reorganisation of research activities and the establishment of a European procurement system). An integrated EDEM would consist of a set of customers served by a set of suppliers trading without restriction. The advantages of such an EDEM for both the supply and the demand side are generally acknowledged: European companies would get a much larger home market, could restructure across national boundaries to reduce duplication, create centres of excellence and take advantage of longer production runs. At the same time, competition would encourage suppliers to optimise production capacity and help to lower costs, and thus save scarce public resources.

The objective of an EDEM has already been set by WEAG. The CPD in particular has laid down a set of principles, addressing specific issues such as cross-border competition and technology transfer on the basis of common procedures. However, these principles have not really been implemented. In particular the attempt to open up markets by establishing national procurement focal points and declaring procurement needs in national official publications has suffered greatly from a lack of binding commitments.⁶³

Drawing on the experience of the single market, the EU could offer additional means to facilitate the realisation of an EDEM. The most efficient way to achieve this objective would be to:

- use first-pillar instruments wherever possible in order to get legally binding and rapidly applicable provisions;
- adapt existing Community law and policies to the specificities of the defence sector;
- analyse systematically which areas of the LoI Framework Agreement can be transformed into Community law.

In its Communications of 1997 and 2003 the Commission has already defined the various areas where action would be needed to

63. Sandra Mezzadri, *op. cit.* in note 19, pp. 10-14.

establish an EDEM based on Community law. The difficulty is the political decision by member states to create such a market rather than its technical implementation. However, it is worth describing briefly the main patterns of an integrated market, if only to put an end to the demonisation of the issue itself.

Procurement law

Existing EU public procurement law for commercial items is based on three principles: Community-wide advertising of calls for tenders, the banning of technical specifications liable to discriminate against potential foreign bidders and the application of objective criteria in tendering and award procedures. Contracts have to be put out to open tender (open to all interested parties) or restricted tender (open to selected candidates), as decided by the authority placing the contract. Only in specified exceptional circumstances may authorities have recourse to negotiated tendering.

It goes without saying that provisions for commercial markets cannot be simply applied to defence goods and services. For example, the complexity of modern weapons systems for which the customer defines detailed technical and operational specifications makes it difficult to assess whether procurement decisions are taken on the basis of 'objective criteria'. Moreover, security of supply and confidentiality are much more important in defence than in commercial markets. However, all this does not mean that it would be impossible to define binding provisions inspired by Community law for an integrated EDEM.

In general, a regulatory framework for European defence procurement should operate at two levels: one for national customers, and a second one for the ARCA.

For national procurement decisions, the application of Article 296 should be restricted to highly sensitive goods. As suggested in the Commission's Communication of 1997,⁶⁴ only cryptography, nuclear, radiological, biological and chemical products should continue to be excluded from European rules. All other products falling under Article 296 and so far exempted should be subject to a specific defence procurement directive.

Such a directive should be based on existing public procurement law but take into account the concerns of member states on the specificity of the defence sector. This means in particular that:

64. 'Implementing European strategy on defence-related industries', op. cit. in note 32.

65. The ownership of IPRs in defence contracts varies greatly between EU member states. The Lol Framework Agreement deals with this issue as well, but only within the creation of a transnational defence company.

- calls for tenders should be organised Community-wide but restricted to companies that have the necessary security certification from their respective national authorities;
- access to technical clauses of tenders, proposals and contracts would be restricted on a need-to-know basis;
- the EU directive must include provisions for IPRs⁶⁵ and security of supply, based on the LoI Framework Agreement;
- for off-the-shelf procurement, offsets,⁶⁶ or at least indirect offsets,⁶⁷ should be prohibited in order to guarantee transparency and open competition.

This procurement directive could be introduced step-by-step, starting with components and subsystems and gradually being enlarged to integrated weapon systems. A gradual approach such as this would make it possible to gain experience with less sensitive items and make adjustments, if necessary, before the directive is fully applied. However, member states and the Commission should, right at the beginning of the process, set a deadline for full application of the directive (for example 2010).

For procurement projects run by the ARCA, OCCAR rules and procedures should apply.⁶⁸ This means, in particular, that competitive tendering and the award of contracts could be extended to non-EU/WEAG members on the basis of reciprocity but also limited to countries participating in a given project. OCCAR's current transitional arrangements, in contrast, should be definitely lifted in order to allow for full application of the principle of global *juste retour*. In general, OCCAR rules would be more flexible than the EU directive, thereby creating an incentive to move procurement decisions from the national to the European level.⁶⁹

Competition law

Existing community competition law contains four main areas of action: (1) merger control, (2) state aid, (3) anti-trust and cartels, and (4) liberalisation. State aid and merger control are of particular interest for their possible application in defence.

As to merger control, Community law already applies to industrial restructuring of defence companies once civilian activities are also concerned. In hi-tech sectors like aerospace and electronics, this is the rule rather than the exception. However, in particular in strategic sectors competition is facing a general dilemma. In these

66. Offsets are practices involving industrial compensation required as a condition of purchase in sales of defence articles and/or services. Offset activities include subcontracting, licensed production, technology transfer, marketing assistance, financial assistance, investments and joint ventures. These activities may generate Offset Credits which themselves may be traded between suppliers and applied to particular programmes.

67. Direct Offsets allow for compensation in goods and services, which are directly related to the project, whereas indirect Offsets are associated with goods and services unrelated to those that are sold.

68. See in particular Chapter VI of the OCCAR Convention, in Burkard Schmitt, op. cit. in note 1, pp. 51, 52.

69. Greater flexibility would come from two sides: first, even applied on a global basis, *juste retour* represents a kind of 'offset' for commonly developed and produced systems. Second, it could be easier to restrict call for tenders to countries participating in a project.

areas, competition normally takes place on a worldwide scale, and only European companies that have attained a critical size are able to compete with the big US groups on global markets. Industrial consolidation is therefore necessary to improve competitiveness. This means, however, that, at least at prime contractor level, European governments will have to accept national, if not European monopolies for strategic assets to sustain a viable EDITB.

On the other hand, these monopolies are easier to accept in defence markets than in other markets, because governments are in an extremely strong position: they are not only the main (if not the only) customers, they also play a unique role as regulators and sponsors. Moreover, they are normally able to invite suppliers from third countries to participate in a tender.

More important will probably be to maintain a minimum of competition in the second- and third-tier supplier base. Driven by new customer demands (system-of-systems approach and network-centric warfare), prime contractors increasingly develop into large system integrators, capable of offering complete solutions even for complex system architectures. This has a profound impact on the relationship between prime contractors and their subcontractors, implying vertical concentration (takeovers of suppliers by prime contractors) and the emergence of strong – if not exclusive – links between prime contractors and subcontractors.⁷⁰ These trends, if taken too far, could eliminate competition at the component and subsystem level and represent a risk for technological innovation.

All of this needs to be taken into account if EU competition rules are to apply to defence. As the Commission has pointed out,⁷¹ there is probably no need to establish a specific directive, but to agree on ‘guidelines’ on how the Community competition rules in general, and the European Regulation on Merger Control in particular, shall apply to the defence sector. In order to provide industry with a stable and transparent framework for consolidation, national governments should work closely with the Commission on the definition of these Community guidelines and undertake not to invoke Article 296 any more.

Concerning state aid, the application of Community law should be politically uncontroversial. In fact, the Commission intervenes only if subsidies distort intra-community trade, which has never been the case in defence so far. The French government, for example, has subsidised GIAT Industries heavily over the last

70. See Joachim Rohde and Markus Frenzel, *op. cit.* in note 3, pp. 84, 85.

71. See Burkard Schmitt, *op. cit.* in note 1, p. 173.

decade but this has never helped the company to win a foreign contract in the face of other European competitors. In fact, most state subsidies for defence companies aim at helping companies to restructure and reduce staff. Having a social character, such subsidies are in any case allowed under the provisions of current EU law.

It might, however, be worth formally stating that national investments in defence research represent legitimate aid, since they encourage both innovation and competitiveness. Competition law in defence must also allow for state aid that preserves adequate security of supply, in particular in highly sensitive areas. This, again, could be formulated in an interpretative guideline.

Transfers

Up until now, EU member states have not made any formal distinction between arms transfers among themselves and arms exports to third countries. In both cases, individual, prior authorisation is required. This involves administrative procedures that are, to say the least, cumbersome, costly and time-consuming (individual licences, import licences, import certificates, delivery verifications, end-user certificates). This practice is a major stumbling block for cross-border cooperation between European industries. Simplification of the system is therefore highly desirable.

In its recent Communication, the Commission suggests the '[alignment of] national licensing systems by adopting the principle of a global authorisation that would apply to intergovernmental programmes and industrial cooperation programmes'. In practice, this would expand the respective LoI provisions to cover all cooperative projects and all EU member states. Within a cooperative programme, individual controls of each transfer would be replaced by only two general controls, one at the moment when the GPL is requested and the second through an audit at the end of the duration of the licence. This approach would streamline procedures and facilitate industrial cooperation considerably.

Taking the dual-use regime as a model, a Community regime could be based on a Council Regulation, outlining control procedures and mechanisms, and a Council Decision, defining the type of products concerned. National authorities would issue standardised GPLs, and the Commission would monitor the technical implementation.

Exports

Most European cooperation takes place in aerospace and defence electronics, i.e. sectors that are heavily export-oriented. The importance of a GPL for them will depend very much on provisions for exports to third markets. In this regard, the LoI Framework Agreement makes a distinction between the six LoI countries and others. Sales of systems jointly produced by some LoI countries to other LoI partners who have not participated in the programme, are no longer considered as 'exports' but as 'transfers'. This means that GPLs create de facto licence-free zones between the six LoI nations for cooperative projects; once a GPL is issued, companies are authorised to sell a given system to all LoI countries without any need for further export licences. Whether a similar provision could be included into an EU-wide GPL, extending the licence-free zone for cooperative projects to all EU member states, remains to be seen. A minimum requirement would probably be to specify in an end-user certificate that the system stays in the respective buyer country.

Concerning exports of cooperatively produced systems to non-LoI countries, the Framework Agreement provides each participant in a given project with a formal veto right. Practical implementation, however, will probably be fairly flexible. For future EU rules, the Commission is proposing to formalise this flexibility. According to its recent Communication, 'a decision to export outside the European Union should take account of the need for prior consultation with the Member States involved in authorizations while recognizing the political responsibility of the final exporting state.'⁷² This approach would generalise the former Schmidt-Debré agreement covering Franco-German cooperation and streamline export procedures considerably. In this context, lifting the formal veto right for all participants would probably be more controversial than applying the regime to all EU member states, because it would de facto still concern only the major producing countries.

An EU-wide regime based on the provisions of the LoI Framework Agreement would offer two advantages. First, it would be relatively easy to implement, since the EU directives could draw directly on the respective LoI provisions. Second, it would make it easier for subcontractors from non-LoI countries to participate in European projects, fostering specialisation and the creation of a truly European DITB.

72. *Ibid.*, p. 178. For a discussion of the LoI Framework Agreement provisions on export procedures, see Burkard Schmitt, *op. cit.* in note 36, pp. 16-22.

Simplification and streamlining are most urgent for cooperative projects. However, one should not forget that system integrators normally draw on an international supplier base even if they produce only for their national government (or for exports). A Community regime for transfers and exports should therefore be progressively extended to nationally produced defence systems. This should start with components transferred to other EU countries; at a later stage, subsystems could be included. The dual-use regime could again serve as a model: for specific components and subsystems, governments could grant EU-wide GPLs to suppliers and limit themselves to controls before the GPL is granted and once it expires. The system integrator using the component would then be responsible for obtaining national authority for possible exports of the final system.⁷³

Such a framework would not represent a common arms export policy. However, it would not only streamline procedures for cooperation but also establish mechanisms for coordination and consultation, which, in turn, might lead progressively to a harmonisation of national export policies.

73. Introducing both directives on procurement and on transfers with components would help in particular small and medium enterprises to access new markets. This is important to foster specialisation throughout Europe and helps companies from non-EU countries to plug into existing industrial networks. At the same time, this approach should be politically less sensitive than regulatory measures that concern the big system integrators.

Since the end of the Cold War, there have been a multitude of initiatives aimed at fostering and improving arms cooperation in Europe. Some of these initiatives contain useful elements, but they are still too limited to overcome the structural deficiencies of Europe's armaments sector, namely fragmentation and duplication.

More far-reaching reforms are urgently needed to achieve greater cost-effectiveness. If not, the dilemma of budget constraints and increasing costs for complex weapon systems will make it extremely difficult, if not impossible, for Europe to maintain a competitive Defence Industrial and Technological Base and improve its military capabilities. Therefore, a coherent policy should be developed in three areas: procurement, research and the defence market.

The EU could be the appropriate framework for developing and implementing such a policy, in particular because of its broad range of Community and CFSP instruments. The Commission's Communication of March 2003 and current plans for a European Armaments, Research and Capabilities Agency (ARCA) therefore offer a unique opportunity to reform Europe's armaments sector.

The creation of an Agency now seems generally accepted. However, important stumbling blocks remain, and the current consensus on the principle might well dissipate when discussion of the details begins. The funding of such an Agency and its actual power, its role vis-à-vis industry, its management rules and the link with the Commission will certainly become bones of contention. It remains to be seen whether consensus on these issues will be easier to reach in the EU (in particular at 25) than it was in WEAG.

Granted, in particular if the creation of the Agency is stipulated in the Treaty, it will be politically difficult to drop the project again. However, the question is what price is to be paid in terms of

efficiency in order to get the necessary political consensus. There are probably two major risks.

- The first one is continuing along the lines of the ECAP process and limiting the activities of the Agency to the short-term capability needs of the Headline Goal Force only. This would exclude the bulk of Europe's military planning, making it impossible for the Agency to exploit its potential and identify all possibilities for cooperation.
- The second risk is that the lowest common nominator prevails, diluting the project to a point where the Agency becomes nothing more than an EU remake of WEAG. Weak structures and non-binding arrangements would then bring little, if any, added value.

Those risks can only be avoided if all EU countries recognise the urgency to act and draw the necessary conclusion. For the sake of cost reduction and interoperability, they must dramatically improve their armaments cooperation even if their foreign and defence policies differ. If common sense prevailed, most solutions would be a foregone conclusion, and one can only hope that financial pressures will be so strong that member states will overcome, for once, national egoism, bureaucratic reflexes and mutual mistrust.

Non-producing countries in particular – which often buy American – must understand that a competitive EDITB is also in their interest, because it is the only safeguard against a US monopoly and thus the only guarantee of attractive US offers. The least they should do is therefore not to prevent the arms-producing countries from using the EU to set up more efficient structures.

As far as the LoI countries are concerned, they should recognise that traditional cooperation schemes are no longer sufficient, and that the surrender of prerogatives in armaments to an EU agency does not mean the end of national sovereignty in defence. This implies also that they should overcome their traditional reluctance vis-à-vis Community instruments and view the Commission as a partner committed to a strong EDITB.

As long as intergovernmental methods prevail, there will always be political limits to cost-effectiveness. However, national sovereignty must no longer be an excuse for non-action at the cost of taxpayers, armed forces and industry. A brief examination of the

ARCA model suggested in this paper shows that innovative solutions can be compatible with necessary national prerogatives, provided member states are serious about their proclaimed intentions:

- ▶ ARCA's range of activities should cover the whole procurement cycle for the development of European projects, but also off-the-shelf acquisition. Organisation and methods should be based on a commercial approach.
- ▶ The ARCA should build on the experience of existing bodies and use existing methodologies and instruments if appropriate. The ECAP mechanism and the LoI boards for harmonisation of military requirement and R&T should be transformed and integrated into the new structure. The OCCAR *acquis* should at least be maintained, and WEAG's EUROPA MOU should become the legal basis for ARCA's R&T activities.
- ▶ To counterbalance as far as possible the difficulties presented by an intergovernmental environment, the ARCA should have permanent working groups, sufficient autonomy, a strong mandate and a direct link to ministers. Moreover, its Director should be a high-level politician rather than a civil servant.
- ▶ The ARCA should monitor *all* relevant capabilities (military, industrial and technological) in a *long-term* perspective. As for military capabilities, ARCA should analyse both EU *and* national planning.
- ▶ To fulfil its tasks, the ARCA should consist of three functional divisions – capabilities, research and procurement – and two units for EDITB monitoring and test facilities respectively. Since ARCA should focus on *future* military needs, close cooperation between capabilities and research divisions would be particularly important. Participation in the various divisions and groups must be flexible.
- ▶ The ARCA should have its own budget for research projects up to the level of demonstrators. This budget should be co-funded by governments, the Community and, possibly, industry. Legal arrangements for research projects should be based on ERG No. 1. The Agency would work in close cooperation with the Commission and/or a future Agency for Strategic Research (ESRA) in order to develop a coherent EU research strategy.
- ▶ OCCAR should become the programme management organisation of the ARCA procurement division. As such, OCCAR

would automatically be in charge of the development, production and in-service support of all projects defined by ARCA 'Project Groups'.

- OCCAR should maintain an (semi-) autonomous status. Its current management rules, principles and membership criteria should persist, and any changes should be decided by OCCAR member states only. At the same time, the Director of the ARCA should chair the OCCAR Board of Supervisors, and the Agency's Executive Director for procurement should be double-hatted, holding also the post of OCCAR General Manager.

An Agency organised along these lines would not be a revolution in armaments affairs, but it could probably generate new synergies and increase efficiency. It would fill the most important gap in Europe's armaments sector, namely the harmonisation of military requirements and its link to cooperation in research. It would allow for flexible participation, cover all phases of the procurement cycle and help OCCAR to exploit its potential fully. Last but not least, it could become an effective interface between member states, on the one hand, and other relevant EU institutions on the other.

This last point is crucial since the success of ARCA will depend very much on the way it interacts with other bodies. First of all, the decision *which* capabilities are needed is first a political and then a military decision that falls beyond the scope of ARCA. In consequence, ARCA can only work efficiently if it gets the necessary input from military planners in member states. Secondly, ARCA should focus on capability- and project-related military research, and leave advanced research to other, more competent bodies. This, in turn, implies close cooperation in particular with the Commission. The latter will certainly try to include advanced strategic research in the 7th Framework Programme (2006 onwards). If the ARCA is set up in 2004, this will be an excellent possibility to start coordinating the respective research programmes.

The Commission will also be the driving force for the future debate on a defence equipment market. Most market issues can be tackled independently of the establishment of the Agency. However, the creation of the ARCA would undoubtedly have a positive impact on the creation of a common defence equipment market. It would not only send a political signal, but also bring in a genuine European actor on the demand side. This would certainly facili-

tate the dialogue between the Commission and member states, in particular if the Director of the Agency were a respected, high-level political personality. Member states should therefore give ARCA an explicit mandate to make recommendations for the adaptation of the community framework.

The establishment of an EDEM is a highly complex endeavour that it has not been possible to discuss in detail here. However, from the author's point of view, the following points are essential.

- An integrated European defence equipment market is indispensable in order to increase competition and create a homogeneous defence economic space. It needs common rules and regulations and can only work if it is based on legally binding commitments. It should therefore be established through the adaptation of existing Community law.
- A common procurement law for defence should be introduced through the limitation of Article 296 to highly sensitive goods. It should apply only to national procurement decisions, whereas the ARCA would be free to set its own rules based on the existing OCCAR regulations. A community directive on defence procurement should be introduced progressively, starting with components and subsystems.
- Based on the provisions of the LoI Framework Agreement, a Community regime for transfers and exports should be established. This regime should cover all cooperative projects as well as components and subsystems integrated into national systems.

If all the steps that are currently being discussed and have been presented in this paper were actually taken, Europe would considerably enhance the efficiency of its armaments sector. However, even if there were sufficient consensus and political will to act, measures could only be implemented progressively. Discussions on the various aspects of an EDEM will continue for some time, along the lines defined in the Commission's Communication. A new organisation for strategic research will not be set up overnight either. As for the creation of the Agency, the consequences of the Thessaloniki Presidency Conclusions for the draft Convention are still unclear. One might be tempted to say that the Articles I-40.3 and III-207 would become superfluous if the ARCA were really set up in 2004. However, there are good reasons to maintain the relevant provisions in the EU Treaty. First of all, it would strengthen the Agency's legal and institutional position if it were mentioned in the

Treaty. Secondly, if attempts to set up the ARCA in 2004 fail, the reference in the Treaty would be useful as a 'reminder' to try it again later. Last but not least, 2004 will probably be only a first step, i.e. the creation of a basic structure that will then have to be developed further. Once the new EU Treaty is ratified, the Council could interpret Articles I-40.3 and III-207 as a mandate to draw the first lessons and eventually to revise the solution arrived at in 2004.

However, the creation of the ARCA is not an end in itself, but rather a means to improve capabilities, enhance competitiveness and increase efficiency through more and better cooperation. Certain principles, like global *juste retour*, should therefore not be negotiable. If there is no satisfactory consensus at 25, those countries that are willing to move ahead should not hesitate to do so outside the EU Agency.

Even then, there would be plenty of possibilities to improve armaments cooperation. The LoI countries, for example, could launch a more ambitious second phase and develop common rules and regulations. OCCAR could easily be transformed into a fully-fledged Agency, and nobody would prevent its member states from (a) broadening OCCAR's scope of activities, (b) giving OCCAR greater autonomy, (c) increasing the number of OCCAR projects and (d) establishing within the OCCAR framework permanent 'Capability Groups' and 'Project Groups'. Certain aspects could also be tackled in other formats (or even bilaterally). Those who consider a European Defence Union to be desirable could, for example, fully integrate their capability planning, establish permanent structures for the harmonisation of military requirements and/or go beyond the current LoI Framework Agreement.

Such developments would, of course, change the scope and the mission of the Agency completely. The latter could then, at best, try to coordinate the various initiatives, and act as an interface between EU and non-EU bodies and as a place-holder for the latter until their transfer into the EU becomes one day possible.

However, this would only be a second-best option. Its only justification would be to prevent the worst case, i.e. a solution inside the EU that would reduce rather than increase efficiency and represent a backwards step as compared with what exists today. The best solution remains a flexible setting within the EU that allows the combined use of Community, CFSP and national instruments for a comprehensive policy.

Member states should therefore enter into constructive dialogue with the Commission on market and research issues and agree, at the outset, on an ambitious concept for ARCA that provides for both flexibility and effectiveness. Such a concept should be possible if governments accept the fact that armaments in Europe is no longer a purely national domain and redefine their national interests accordingly.

Abbreviations

A400M	Airbus-400M Transport Aircraft
AHSG	Ad Hoc Study Group
ARCA	(European) Armaments, Research and Capabilities Agency
B	Belgium
BoS	Board of Supervisors
CEN	European Committee for Standardization
CEPA	Common European Priority Area
CFSP	Common Foreign and Security Policy
COARM	Conventional Arms Exports Working Group
COREPER	Committee of Permanent Representatives
CPD	Coherent Policy Document
DARPA	Defense Advanced Research Projects Agency
DDI	Developing Defence Industry
DG	Directorate-General
DITB	Defence Industrial and Technological Base
E	Spain
EA	Executive Administration
EAA	European Armaments Agency
EC	European Commission, European Community
ECAP	European Capabilities Action Plan
ECT	European Community Treaty
EDEM	European Defence Equipment Market
EDITB	European Defence Industrial and Technological Base
E.P.A.SE.RE.TE	EU Cooperation Programme for Advanced Research and Technology
ERG	European Research Grouping
ESDP	European Security and Defence Policy
ESRA	European Strategic Research Agency
EU	European Union
EUCLID	European Cooperation for the Long Term in Defence
EUMC	European Union Military Committee
EUMS	European Union Military Staff
EUROPA	European Understandings for Research Organisation, Programmes and Activities
FP	Framework Programme
FR	France
FSAF	Future Surface-to-Air missiles Family

GDP	Gross Domestic Product
GE	Germany
GMES	Global Monitoring for Environment and Security
GNE	Group of National Experts
GPL	Global Project Licence
GRD	Group of Research Directors
IEPG	Independent European Programme Group
IGC	Intergovernmental Conference
IPR	Intellectual Property Rights
IT	Italy, Information Technology
LoI	Letter of Intent
MOD	Ministry of Defence
MOU	Memorandum of Understanding
MTCR	Missile Technology Control Regime
NAD	National Armaments Director
NATO	North Atlantic Treaty Organisation
OCCAR	Organisation for Joint Armaments Cooperation
PSC	Political and Security Committee
POLARM	European Armaments Policy Council Working Group
R&D	Research and Development
R&T	Research and Technology
SGTF	Sub-Group on Test Facilities
T	Turkey
TA	Technical Arrangement
TDC	Transnational Defence Company
TEC	Treaty establishing the European Community
TEU	Treaty on European Union
UK	United Kingdom
US	United States of America
WEAG	Western European Armaments Group
WEAO	Western European Armaments Organisation
WEU	Western European Union

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Up until now, EU member states have excluded armaments from the European integration process and have cooperated in this field outside the EU framework. However, there is a fair chance today that this will change: both the work of the Convention on the Future of Europe and the debate on the recent Commission Communication on a common defence equipment policy indicate a greater openness among national governments vis-à-vis possible EU involvement in armaments.

This *Chaillot Paper* argues that the EU could indeed play a useful role in the necessary reform of Europe's armaments sector, because it could develop a more coherent institutional setting and bring in a broad set of relevant Community and CFSP instruments. Both could help to implement a comprehensive strategy in those three areas where action is mostly needed: procurement, research and the defence market.

Granted, even if the EU develops an armaments dimension, member states will certainly continue to be reluctant to surrender national prerogatives. This will inevitably put limits on any improvements in cost-effectiveness. However, this paper suggests that innovative solutions are possible provided governments are serious about their declared intentions.

Drawing on lessons from existing cooperative arrangements, the paper develops in particular a blueprint for the proposed European Armaments, Research and Capabilities Agency, and shows how it could work. Moreover, it presents an outline for a European Defence Equipment Market based on Community law and gives some indication of how it could be formed.

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