

EXPLANATORY MEMORANDUM ON EUROPEAN UNION DOCUMENT

COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE EUROPEAN COUNCIL, THE COUNCIL, THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE AND THE COMMITTEE OF THE REGIONS: REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL ESTABLISHING THE EUROPEAN DEFENCE INDUSTRIAL DEVELOPMENT PROGRAMME AIMING AT SUPPORTING THE COMPETITIVENESS AND INNOVATIVE CAPACITY OF THE EU DEFENCE INDUSTRY.

Submitted by the Ministry of Defence, 10 July 2017

SUBJECT MATTER

1. This Commission Communication proposes a Regulation establishing a European Defence Industrial Development Programme (EDIDP). The EDIDP is part of the larger European Defence Fund (EDF) covered by a further Explanatory Memorandum submitted separately. By part funding the collaborative development of defence capabilities, the EDIDP aims include encouraging cooperation between member states and the defence industry; and helping to tackle the so-called valley of death between research activity and the acquisition of defence capabilities.
2. The current EDIDP Regulation will last for two years, with the Commission aiming to spend €245 million in 2019 and €255 million in 2020. For the next Multinational Financial Framework (MFF), negotiations for which are due to commence in 2018, the Commission proposes to spend €1 billion per annum on the EDIDP. In order to ensure a successful EDIDP and accordingly strengthen the argument for the next MFF, the Commission is keen to have the Regulation approved by Council and Parliament by the end of 2017 and for member states to identify potential cooperative topics as soon as possible.
3. Under the EDIDP the Commission will fund up to 20% of the costs of the collaborative development of defence capabilities, rising to 30% for projects developed in the framework of Permanent Structured Cooperation; with member states contributing the rest. The capabilities priorities available for EDIDP funding will be advertised in a Commission programme of work. To apply consortia must be made up of a minimum of three undertakings from two or more member states and who can show that the rest of the funding will be provided by member states. The funding will go direct to the members of the consortia rather than to the member states.

SCRUTINY HISTORY

4. On 21 February this year the MOD submitted Explanatory Memorandum 15160/16, COM(2016) 950 (*Commission Communication: European Defence Action Plan*) to both Commons and Lords EU Committees. This was the first reference to

the European Defence Fund. The House of Lords EU sub-committee cleared the document from scrutiny on 22 March 2017. The House of Commons European Scrutiny Committee cleared the document from scrutiny but requested further information. It also drew the document to the attention of the Defence Committee. The additional information was provided in July 2017.

MINISTERIAL RESPONSIBILITY

5. The Secretary of State for Defence has overall responsibility for policy on Defence research, capability and procurement. The Secretary of State for Foreign and Commonwealth Affairs, the Chancellor of the Exchequer, Secretary of State for International Trade and the Secretary of State for Business, Energy and Industrial Strategy also have an interest.

INTEREST OF THE DEVOLVED ADMINISTRATIONS

6. Defence is a reserved matter under the UK's devolution settlements, but the devolved administrations have an interest in European defence industrial policy and have been consulted in this Explanatory Memorandum.

LEGAL AND PROCEDURAL ISSUES

7. Legal basis: Article 173 of the Treaty on the Functioning of the European Union concerning the competitiveness of EU Industry. MOD lawyers have advised that there are some doubts over the proper reach of this Article into the domain that is covered by Article 45 of the Treaty on the European Union, which specifies the European Defence Agency's (EDA) lead role in defence research. There is also a question as to whether this legal base may limit the extent that EU funding can be used by the Commission for research that is defence-specific. The Commission are confident that this is not the case. These points will continue to be assessed as the Regulation develops.

8. European Parliament Procedure: the Ordinary Legislative Procedure.

9. Voting procedure: Qualified Majority Voting.

10. Impact on United Kingdom Law: none.

11. Application to Gibraltar: yes.

12. Fundamental rights analysis: no issues.

APPLICATION TO THE EUROPEAN ECONOMIC AREA

13. None.

SUBSIDIARITY

14. Defence is a national competence, however, action at the European level is appropriate here as the resources involved in developing defence capabilities are regularly too high for countries to pursue individually so cooperation is often a necessity. Moreover, while the defence industry is becoming increasingly international there is still significant duplication and fragmentation across national borders, which impedes the internal market and adds significant costs to defence.

Action at the European level can reduce these barriers thus strengthening the UK and European Defence Technological and Industrial Base. However, it must be noted that there is a competency constraint on the EU under Article 346(1) TFEU, which protects member state autonomy over measures in the essential interests of its security which are connected with the production of or trade in arms, munitions and war material. Close attention will be paid to the development of this programme, in particular as it applies to common standards, to maintain the role of the EDA and ensure nothing interferes with member state autonomy in these areas.

POLICY IMPLICATIONS

15. The Government broadly welcomes the general intent of the EDIDP to strengthen Europe's defence capabilities and the defence industry, but we also have a number of concerns and points that require further clarification. These include:

The draft Regulation appears to give the Commission significant influence to shape future defence capability priorities. We believe there is more work required on programme governance to ensure balance with member states defence competence.

We believe the rule that member states or nationals of member states must own over 50% of the undertaking for it to qualify for funding is inappropriate in the context of international shareholders and attracting new investment.

The provision that all assets and resources used by the participants, including subcontractors, funded under the EDIDP are not to be located in the territory of non-Member States is overly protectionist and unrealistic.

The Regulation says nothing on the involvement of countries outside the EU.

16. Since the EDIDP will most likely reduce the contribution required from participating member states in a programme rather than provide an added windfall for the defence industry, further clarification is required on what the EDIDP will incentivise in practice. Nor is it clear who will be the independent experts who will assist the Commission in the assessment of proposals; the role of the European Defence Agency, if any, in managing the implementation of the Programme; and which other entity the Commission envisages delegating some of the implementation tasks.

17. The Government intends to ensure the above interests and concerns are addressed as the EDIDP proceeds through the legislative process. We will continue to work with our EU allies, including our Letter of Intent partners, France, Germany, Italy, Spain and Sweden, who share many of our industrial interests.

18. Turning to the matter of our exit and our future involvement to the EDIDP. As it stands EDIDP funding will only be available to EU undertakings. There is a risk that the EDIDP could be used in a way that disadvantages the UK and the UK defence industry through, for example, only considering collaborative programmes made up of EU member states or preventing proposals from consortia that include UK companies in their supply chains.

19. The level to which we participate in the EDIDP post our exit will be a matter for our negotiations. During those negotiations the Government believes that it is in both ours and the EU's interests for us to have a positive relationship on the EDIDP.

CONSULTATION

20. In addition to consulting member states, the Commission has consulted the defence industry closely, in particular through the Aerospace and Defence Industries of Europe trade organisation of which the UK Aerospace Defence Security and Space trade organisation is a member.

IMPACT ASSESSMENT

21. In view of the tight timescales the Commission claims to have been unable to undertake an impact assessment. With the EDIDP coming into effect as we leave the EU the impact on the UK and UK defence industry is dependent on the result of UK-EU negotiations.

FINANCIAL IMPLICATIONS

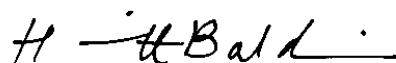
22. There are no new financial commitments resulting from the Programme. Since the EDIDP will only commit resources from 2019 onwards, almost all of the expenditure arising from the current MFF up to 2020 will be incurred after we have left the EU. Accordingly, the exact financial implications are dependent on the UK-EU exit negotiations.

23. The EDIDP will be funded using money from various other programme budgets (including Galileo and Copernicus). It is proposed that €135 million from the Galileo budget for this new Programme which has raised some concerns from the UK Space Agency but is considered manageable based on current expenditure plans.

24. The budget for any follow on EDIDP in the next MFF (2021 onwards) will be a matter for the EU member states. Specific financial implications for the UK will be dependent upon what if any arrangement the UK has with the EDIDP.

TIMETABLE

25. The EDIDP was announced on 7 June 2017. The Commission has stated it wishes for the Council and Parliament to approve the Regulation by the end of 2017 in order to fund projects in 2019. The 22-23 June 2017 European Council has called for its rapid agreement with a view to its swift implementation.



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Parliamentary Under Secretary of State and
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