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UK Defence Procurement Policy

The UK spends, on average, £9-10 billion on defence procurement each year. Following consistent criticism from the National Audit Office of inefficiencies within defence procurement spending, the Strategic Defence Review (SDR) in 1998 sought to streamline the procurement process in order to minimise overspend and delays in MOD equipment programmes.

This paper examines the key elements of the Smart Procurement Initiative introduced under the SDR and its development in the last five years. It also outlines the key multinational efforts the UK has been involved in to streamline procurement and address capability shortfalls, including the NATO Prague Capabilities Commitment, the European Capabilities Action Plan and the establishment of the Organisation Conjointe de Coopération en matière d'Armement (OCCAR).

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Summary of main points

The UK spends on average £9-10 billion on defence procurement each year. Previous Governments have consistently struggled to deliver key equipment capabilities within agreed costs and timescales. In 1997 the National Audit Office reported that the 25 largest defence equipment projects underway at the time were forecast to cost over £3 billion more than originally planned and would, on average, enter service over three years late.¹

A key element of the 1998 Strategic Defence Review (SDR) was a re-examination of the procurement process from both an organisational and a procedural perspective. The Smart Procurement Initiative (SPI) was launched with the aim of establishing a closer customer/supplier relationship and delivering equipment ‘faster, cheaper and better’.

Under SPI the procurement of equipment would be undertaken on a ‘through-life’ basis, from the concept phase of a capability through to its support once in Service. Incremental acquisition would be introduced as a procurement option in order to achieve initial capability more quickly with a view to upgrading equipment in line with technological advancements while in-Service. The Procurement Executive within the MOD would be given Agency status and Integrated Project Teams (IPTs) would be established to bring together the main stakeholders for the life of the programme. A dedicated customer would also be established within the MOD Central Staffs. The equipment approvals process would be streamlined to allow for greater focus on risk mitigation during the early phases of a project. The main decision-making points in the procurement cycle would be reduced from three to two. The SDR envisaged that SPI measures would save £2 billion over ten years.

The SPI was re-launched as Smart Acquisition in October 2000. Smart Acquisition was intended to refine and develop the SPI concept and to “stress the point that the MOD is concerned not only with buying equipment, but with acquiring the means to support it throughout its in-service life.”² Under Smart Acquisition every project would be assessed at the outset for its viability under the Private Finance Initiative.

As an increasing part of the procurement budget is devoted to collaborative projects the UK has been keen to promote the principles of Smart Acquisition within multinational projects and organisations such as the Organisation Conjointe de Coopération en Matière d’Armement (OCCAR). Priority has also been given to addressing capability shortfalls through the NATO Prague Capabilities Commitment (PCC) and the European Capabilities Action Plan (ECAP).

In October 2002 the MOD published its Defence Industrial Policy which seeks to link up current industry and government initiatives and to provide a clearer framework for the defence procurement process, for defence research and development, and for maximising the future competitiveness of the UK defence industry.

¹ National Audit Office, *Ministry of Defence: Major Projects Report 1997*, HC 695, Session 1997-98

² *Defence Acquisition*, MOD Policy Paper No 4, December 2001.

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I The Strategic Defence Review

The National Audit Office (NAO) *Major Projects Report 1997* highlighted that the 25 largest defence equipment projects underway at the time were forecast to cost over £3 billion more than originally planned and would, on average, enter service over three years late; a situation unchanged from the NAO's previous assessment in 1996.³

The main causes of procurement problems were identified by the MOD as:

- slippage: due to technical difficulties, budgetary constraints leading to the postponement of expenditure, the redefinition of requirements and difficulties over collaborative programmes;
- cost over-run: due to programme changes, changes in equipment specification, poor estimating and inflation of prices for defence equipment in excess of inflation in the economy as a whole.⁴

The type of threats faced by the UK's Armed Forces were also regarded as increasingly diverse and less predictable, therefore requiring new technology requirements to be deployed more quickly. The length of the existing procurement cycle was regarded as problematic as new programmes were unable to keep pace with the rate of technological change.

One analyst commented:

The defence ministry's capacity to waste money is legendary. Procurement is a dismal story of delays and extortion. The defence contractors, assured their prosperity is vital to national security, have a captive customer and no incentive to cut costs.⁵

Consequently, reform of defence procurement policy was identified as one of the main objectives of the MOD's Strategic Defence Review (SDR) when it was announced in May 1997.

A. The Smart Procurement Initiative (SPI)

The key procurement development to come out of the SDR was the Smart Procurement Initiative (SPI), which aimed to establish a new customer/supplier relationship between the MOD and industry and to deliver equipment 'faster, cheaper and better'.⁶ The then

³ National Audit Office, *Ministry of Defence: Major Projects Report 1997*, HC 695, Session 1997-98

⁴ Ministry of Defence, *The Strategic Defence Review: Supporting Essays*, July 1998, Essay Ten, Para 4

⁵ Philip Stephens, "Short range target: Tony Blair's defence review has taken the politics out of the issue but has missed the opportunity to think 10 years ahead", *The Financial Times* 25 May 1998

⁶ Ministry of Defence, *The Strategic Defence Review*, Cm 3999, July 1998, para 161

Parliamentary Under Secretary of State for Defence, John Spellar, described the initiative thus:

The Defence Review identified better ways of buying and maintaining equipment, and supporting the Armed Forces. Overall, we spend some £9 billion a year on defence equipment, spares and stores. In the Review we launched the Smart Procurement Initiative to get better and cheaper equipment faster, and to work more effectively in partnership with industry, rather than the sterile confrontation of the past. It lies at the heart of our agenda to modernise Defence and the Armed Forces.⁷

The key elements of the SPI were as follows:

- The introduction of a “through-life systems approach” covering both initial acquisition and in-service management of equipment. This approach would be embodied by the establishment of Integrated Project Teams (IPTs) bringing together the main stakeholders for the life of the project. Industry would be part of the IPT except during the competitive evaluation phase. IPTs are covered in greater detail in section B.
- More comprehensive project planning earlier on in the procurement cycle with appropriate trade-offs between military requirements, time and costs in an effort to assuage later cost overruns and delays.
- Partnering arrangements with industry, particularly where open competition on a programme was considered to be unviable.
- The introduction of new procurement techniques including incremental acquisition whereby equipment would be initially accepted into service with less ambitious capability and subsequently upgraded in lower-risk steps. This approach would allow greater flexibility in the incorporation of advancements in technology during the lifetime of a programme.
- Improved commercial practices, including greater incentives for contractors, fixed price contracts for programmes up to five years duration and greater consideration of contractor past performance in the evaluation of tenders.⁸

The SDR envisaged that its SPI measures would save £2 billion over ten years.⁹

⁷ MOD Press Release, 31 March 1999

⁸ Ministry of Defence, *The Strategic Defence Review: Supporting Essays*, July 1998, Essay Ten, Essay Ten, para 8

⁹ *ibid*, para 21

B. Organisational Change

The SDR also examined the position and role of the Procurement Executive (PE) organisation within the MOD and whether the SPI could be delivered by either an in-house specialist procurement body or within the private sector. The SDR concluded that the requirement remained for an in-house defence procurement body, albeit one that was more commercially focused and with a more closely defined relationship with its customer. The review recommended that this could be best achieved by turning the PE into an Agency and establishing a new central customer in MOD HQ. Changes to the PE were expected to achieve a reduction in operating costs of around 20% by 2001-02.¹⁰

1. Equipment Capability Customer (ECC)

The role of the Equipment Capability Customer (ECC) envisaged under Smart Procurement would be to determine equipment capability requirements in order to meet the current and future needs of the Armed Forces. The Directors of Equipment Capability (DEC) within the ECC would act as the primary customer and liaison point for the Integrated Project Teams (IPT) within the Defence Procurement Agency (DPA) and the Defence Logistics Organisation (DLO). The relevant DEC, in conjunction with an IPT, would agree from the outset the relevant time, cost and performance parameters and any accepted trade-offs between them. The DEC would also act as the acceptance authority for a capability ready to enter service.

An MOD Policy Paper summed up the role of the ECC as follows:

[to] define the requirement; prioritise and balance investment between and within equipment capabilities; seek and obtain approval for the capability; and finally, authorise acceptance by confirming that the capability has been met by the systems supplied.¹¹

2. Defence Procurement Agency (DPA)

The Defence Procurement Agency (DPA) was launched on 1 April 1999. The Agency was to have a slimmed down top management structure which would remove the previous hierarchies and place IPTs at the centre of its work. The IPTs would, in turn, be directly accountable to the DPA Executive Board. The then Chief Executive of the DPA and Chief of Defence Procurement, Sir Robert Walmsley, commented:

Fundamental to this change is shortened reporting chains. For most IPTs this means they will report directly to the Executive Board which will itself be

¹⁰ Defence Select Committee, *The Strategic Defence Review*, HC 138, 10 September 1998

¹¹ *Defence Acquisition*, MOD Policy Paper No 4, p5, December 2001.

collectively responsible - with me as the Chief Executive- for the achievement of the agency's overall key targets.¹²

a. *Integrated Project Teams (IPTs)*

The IPT concept of bringing together the main stakeholders in a programme, including the MOD, Armed Forces and industry,¹³ was considered to be the most efficient method for delivering the 'through life approach' envisaged under SPI. It was hoped that closer co-operation at the outset of a project would lead to earlier identification of potential risks and the more efficient development and oversight of a project throughout its life.

The IPT would be responsible for delivering equipment solutions to meet the requirements of the ECC. It would also be responsible for the equipment programme throughout its life, transferring to the DLO (see below) during the manufacture phase and immediately prior to the equipment entering service. Related equipment capabilities could conceivably be grouped together within a 'cluster IPT'.

A leader would be appointed to each IPT (IPTL) and would have authority over the programme. Most IPTs would also have a Requirements Manager to act as a bridge between the IPT and the ECC and an Integrated Logistics Support Manager to liaise with the DLO to ensure that the IPT delivered the most appropriate in-service support strategy from the outset.

In November 1998 a number of equipment programmes were selected for a three-month trial period to pilot the basic concepts of the SPI. The initial batch of pilot projects were: the Future Attack Submarine (FASM); Joint Battlespace Digitisation; the Future Offensive Air System (FOAS); Nimrod MRA4 and Active Search Sonobuoy System (ASSS); Brimstone; Future Carrier; Dismounted Close Combat Cluster; Combat Vehicle Reconnaissance (T) – LEP; Type 23 Frigate; Apache Attack Helicopter; and the VC10 Tanker and Transport Aircraft.¹⁴

Toward the end of the trial period the then Secretary of State for Defence, George Robertson, provided an assessment of their success:

The 10 pilot projects where we have been trialling Smart Procurement techniques and the IPT concept are already starting to indicate new savings running to several hundreds of millions of pounds over their life. They have also identified significant opportunities to get equipment into service faster, or--for equipment already in service-- improve its availability and reliability. For example, the Type 23 frigate IPT is looking to reduce the length of an upgrade programme by 30 per cent and the VC10 IPT has already identified initiatives to achieve a 10 per cent

¹² Interview with Sir Robert Walmsley, *Preview*, 1 April 1999

¹³ Industry would remain involved in the IPT only during the non-competitive stages of a programme.

¹⁴ Ministry of Defence Press Release, 256/98, 23 October 1998

increase in serviceability. Soon after Easter we will launch the first wave of IPTs covering 23 projects or groups of projects in the DPA and DLO. Over the course of the coming year, the remainder of projects will migrate to this new structure, with a total of about 150 Teams forming in all, some 90 in the DPA and 60 in the DLO.¹⁵

Between April 1999 and April 2000 all other MOD equipment projects were transferred into the IPT structure. The first wave consisted of 23 projects and included major systems such as Eurofighter, Challenger 2 tank, Ground Based Air Defence (GBAD), Beyond-Visual-Range Air-to-Air Missile (BVRAAM), Advanced Short-Range Air-to-Air Missile (ASRAAM) and Bowman.¹⁶

3. Defence Logistics Organisation (DLO)

The Defence Logistics Organisation (DLO), in tandem with the DPA, was launched on 1 April 1999. Its objective was to bring together the three single Service logistics organisations and to establish a consolidated approach to the in-service management of defence equipment and stores, as part of the ‘through life approach’ of Smart Procurement. The SPI envisaged that an IPT would transfer to the DLO toward the end of the manufacture phase of a programme and remain there through to the point at which the asset was disposed of.

The DLO was also tasked with streamlining logistics management, promoting best practice and rationalising stock holdings within each of the Services.

At the launch of the DLO the then Chief of Defence Logistics, General Sir Sam Cowan, stated:

The creation of a Chief of Defence Logistics and the launch of the Defence Logistics Organisation are changes of huge significance for defence. Since the end of the Cold War a great deal of rationalisation and efficiency has been delivered under the current single Service logistics structures but we have done all that can be done within the current context. To deliver greater value we must change the context and that is exactly what the Defence Logistics Organisation is intended to do. We have one huge incentive to succeed since the efficiencies we achieve will contribute directly to the modernisation plans of our forces.¹⁷

¹⁵ HC Deb 31 March 1999, cc677-9w

¹⁶ The full list of Wave 1 IPTs comprises: Roll-on Roll-off ferries; Royal Fleet Auxiliary Support; Seawolf; Challenger 2; Ground Based Air Defence (GBAD); Medium Range Trigat; Combat Support Vehicle (CSV) Support; Eurofighter; Beyond Visual Range Air to Air Missile (BVRAAM); Harrier (JF2000); Sea King; Puma/Gazelle; Conventionally Armed Stand Off Missile (CASOM); Future Anti Surface Guided Weapon (FASGW); Advanced Short Range Air to Air Missile (ASRAAM); Aerial Target Systems; Directional Infrared Countermeasures (DIRCM); Airborne Sensors & Avionics; Air Command & Control; Flight Simulation & Training Systems; Airborne Communications & Homing; Air Armament Equipment; and Bowman. Ministry of Defence Press Release, 023/99, 27 January 1999

¹⁷ MOD Press Release 31 March 1999

The then Defence Secretary, George Robertson, commented on the DLO's aims in a Written Answer on 31 March 1999:

We expect the DLO to make significant improvements in our logistic support, for example: in the ways we procure, manage, repair and store defence munitions; in the procurement and management of fuel; and in the use of lean support techniques. We hope to be able to make further announcements here in the coming months. We are also committed to delivering major reductions in our current holdings of non-explosive stores and to rationalisation of our stock procurement, leading to reductions of £130 million a year from 2001-02 onwards.¹⁸

A central strategic objective of the DLO was to reduce the cost of its outputs by 20% by 2005. A series of business improvement initiatives across the entire range of DLO activities were introduced to achieve this:

- **Resource Accounting and Budgeting (RAB)** – To enable the MOD to understand the true costs of owning equipment, stocks and capital assets.
- **Defence Stores Management Solution (DSMS)** – To give “full visibility of stock across the entire Defence supply chain”.¹⁹ This would allow improved forecasting and offer a deployed capability for front-line operations.
- **Convergence** – A single logistics organisation offered substantial opportunities to streamline processes and spread best practice. A number of significant organisational changes have resulted from this convergence. These have included: an integrated military aviation support capability (Director General Equipment Support (Air)); the Defence Communications Services Agency, which absorbed elements of the RAF Signals Engineering Establishment; the Warship Support Agency (formed on 2 April 2001), which brought together the Ship Support Agency and functions previously carried out by the Naval Bases and Supply Agency; and the establishment of a single Defence Munitions Group.

¹⁸ HC Deb 31 March 1999, c677-9w

¹⁹ *Defence Acquisition*, MOD Policy Paper No 4, p8, December 2001.

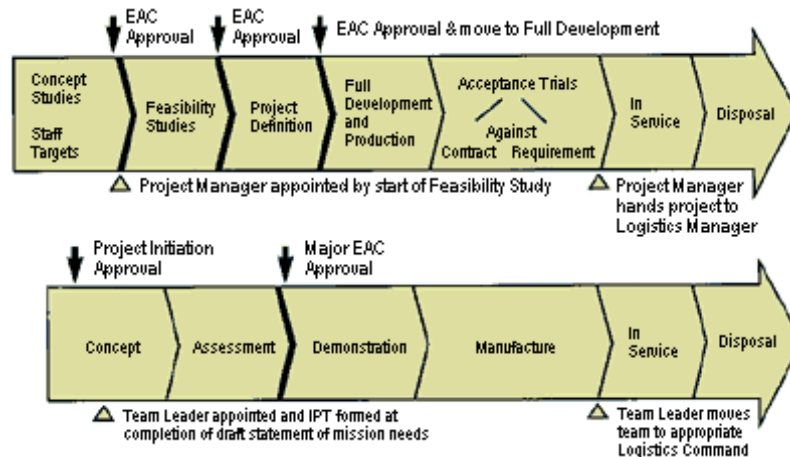
C. Equipment Approvals Procedure

In line with a reassessment of the organisational structure of the MOD with respect to procurement, an evaluation of the equipment approvals procedure was also undertaken as part of the SPI, in order to identify where efficiencies could be achieved.

The SDR acknowledged that during the Cold War pressure existed within the MOD for projects to be quickly pushed forward into development and production in order to meet a specific Soviet threat, despite the fact that significant risks remained. The SDR concluded that a change in the post cold war strategic environment allowed for greater time to be invested in the early concept and assessment phases of a programme, thereby reducing risk. The SDR also acknowledged that the nature of the approvals process had contributed in the past to extending the length of the project.

Therefore, the SDR recommended that the approvals process be simplified. The procurement cycle would be consolidated into six main phases with the main decision-making points in the project cycle reduced from three to two: at the initiation of a project and prior to the main investment in a programme. Greater responsibility would be placed with the relevant DEC and IPTL who would present their recommendations to the main approvals authority, the Equipment Approvals Committee (EAC),²⁰ at the point of main investment. Ministers would continue to take the decisions on larger or potentially contentious projects.

The following diagram outlines the MOD's pre-1998 procurement "Downey cycle" and the acquisition cycle envisaged under the SPI:



Source: Ministry of Defence, *Strategic Defence Review: Supporting Essays*, July 1998, Essay Ten

²⁰ The EAC is the body responsible for the central scrutiny of all equipment requirements. The EAC is chaired by the Chief Scientific Adviser and includes the Chief of Defence Procurement, the Vice Chief of the Defence Staff, the Chief of Defence Logistics and the 2nd Permanent Under Secretary of State.

D. Initial Assessment of Smart Procurement

The *Major Projects Report 2000* was the first formal assessment by the National Audit Office of defence procurement under the SPI. The report concluded:

The Major Projects Report 2000 does present some evidence to judge whether the disciplines of Smart Procurement are beginning to lead to improved performance. However, it is very early to expect to see any major impact on the projects in the report, all of which were begun before the introduction of Smart Procurement [...]

- Forecast costs are 0.2 per cent (£78 million) lower than last year - 5.7 per cent (£2.4 billion) higher in total than at main investment approval - and newer projects are showing less cost overrun per year than older projects. Most of the reduction in the last year relates to future expenditure and includes a £62 million saving on the Eurofighter programme which is dependent on successful contract negotiations;
- The average project delay is getting longer - on average, in-service dates have slipped by 3 months since last year to 28 months in total, against the timetables set at main investment approval. Seven projects experienced delays totalling 63 months in the last year and slippage will increase if the risks allowed for in approvals materialise;
- Delays have led to capability shortfalls on 13 projects.²¹

On the publication of the report the Head of the National Audit office, Sir John Bourn, stated:

I welcome the encouraging signs that the Ministry of Defence is improving cost control on major projects and in future Major Projects Report I will look to see that this improvement is sustained. It is also reassuring that the Ministry of Defence is expecting to meet the technical requirements for new equipment for the Armed Forces. However, that equipment is not always available on time is a concern and it is disappointing that the average project delay is getting longer. The Ministry of Defence must translate the improvements on cost that are coming through under Smart Acquisition to time as well and must reduce project delays.²²

²¹ National Audit Office, *Major Projects Report 2000*, HC 970, 22 November 2000

²² National Audit Office Press Notice. Available online at: <http://www.nao.gov.uk/pn/9900970.htm>

In its report on *Major Procurement Projects* in July 2000 the Defence Select Committee commented:

It will inevitably take some time to see hard evidence of any improvements flowing from the smart procurement initiative. There are, however, it seems to us, some early signs of a more imaginative and robust approach emerging, and these offer a glimpse of what improvements the initiative may be able to provide.²³

David Moore and Peter Antill, writing in the *RUSI Journal*, suggested:

It is hoped that these ‘radical changes... will deliver a forward looking organisation using up to date acquisition processes and procedures. The emphasis will be on flexibility... and continuous evaluation to avoid any danger of stagnation. ‘Faster, better, cheaper’ has become the new catchphrase for the supporters of change but for others, the change in mindset is almost too big to be practical. For them, SMART could be said to stand for Same Methods Appearing Rather Trendy.²⁴

On the concept of the IPT, Moore and Antill commented:

Industry must remain motivated, so that it will enter a dialogue with the MOD during the early stages of a project, so it can gauge requirements quickly and accurately. If this is not achieved, it is unlikely that equipment will be delivered on time, to specification or budget, and it will appear that the new procurement system is no better than the last [...]

Integration of internal stakeholders is essential for the IPTS success. Early signs have been that this may not always be possible.²⁵

²³ Defence Select Committee, *Major Procurement Projects*, HC528, 6 July 2000

²⁴ David Moore and Peter Antill, “Integrated Project Teams: The MOD’s New Hot Potato?”, *RUSI Journal*, February 2000

²⁵ *ibid*

II Smart Acquisition

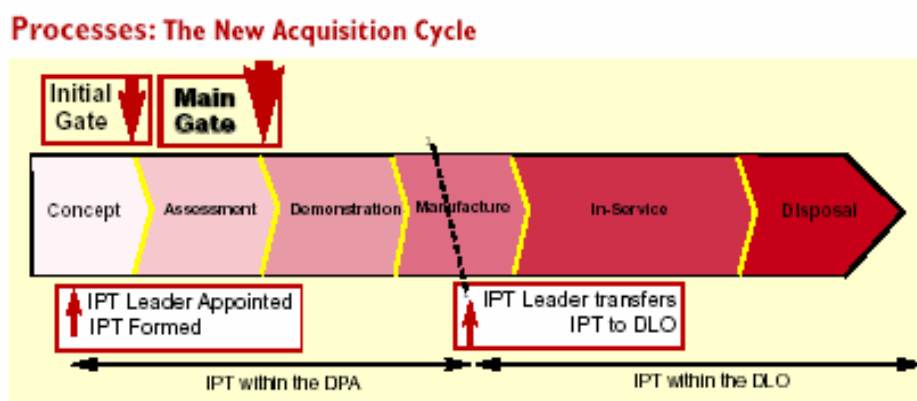
The Smart Procurement Initiative was renamed Smart Acquisition in October 2000. Smart Acquisition was intended to refine and develop the SPI concept and to “stress the point that the MOD is concerned not only with buying equipment, but with acquiring the means to support it throughout its in-service life.”²⁶

The specific objectives of Smart Acquisition, as set down in the MOD’s *Defence Acquisition Policy Paper* of 2001, are:

- Delivering projects which meet or better the time, cost and performance targets which were set when the decision to proceed with the project was made.
- Acquiring capability progressively, at lower risk, and with the right balance between military effectiveness, time and whole-life costs.
- Cutting the time for key technologies to be introduced into the front-line, where needed to secure military and industrial advantage.²⁷

A. The Acquisition Cycle

Under Smart Acquisition, the procurement cycle continues to be a whole life approach, from the concept and pre-development phase of a capability through to its disposal. The expectation remains that a greater proportion of project expenditure would be released during the early stages of a programme in order to mitigate risk and attain a higher level of confidence that project targets for time, whole-life cost and performance, as originally laid down by the DEC and the IPTL, would be achieved at ‘Main Gate’.



Source: *The Acquisition Handbook*, 4th Edition, January 2002

²⁶ *Defence Acquisition*, MOD Policy Paper No 4, December 2001.

²⁷ *ibid.*

From an approvals perspective the Concept Phase through to Demonstration and Manufacture are the key stages:

- **Concept Phase** – A User Requirements Document (URD) is issued by the ECC outlining the user’s needs for a particular capability. An IPT is established, or an existing, related IPT is tasked to deliver the programme. Industry would also be involved at this stage. Expressions of Interest (EOI) would be sought from interested companies/consortia, while Feasibility Studies may also be awarded. The aims of the Concept Phase are to identify technology and procurement options that warrant further investigation and to obtain funding and to identify the performance, cost and time parameters for the programme. The potential for international collaboration would be considered during the Concept Phase, as would the programme’s potential as a PFI (see section II B) and the viability of incremental acquisition. Up to £10 million or 2% of the procurement cost, whichever is the lower, could be spent during the Concept Phase, without approval from the Investment Approvals Board (IAB), which replaced the EAC in April 2002 as the main approvals authority.²⁸
- **‘Initial Gate’ Review** – At the end of the Concept Phase the ‘Initial Gate’ review assesses the feasibility of the programme. IAB approval is required before funds are released for the assessment phase. Approval of a project at ‘Initial Gate’ does not, however, commit the ECC or the IAB to ‘Main Gate’ approval of the programme.
- **Assessment Phase** – A Systems Requirement Document (SRD) is produced, defining what the system must do in order to meet the user’s needs as stated in the URD. Invitations to Tender (ITT) would be issued to industry and Assessment Phase contracts subsequently awarded to a short-listed number of companies or consortia. A further down-selection of bidders during this stage is a possibility. Industry involvement in the IPT would be suspended once the ITT is issued. The mitigation of risk continues to be a major objective with up to 15% of the initial procurement cost of a capability spent, on average, by the end of the Assessment Phase. Trade-offs between cost, time and performance occur mainly during this phase, before the Main Gate review and as the URD and SRD evolve.²⁹
- **‘Main Gate’ Review** – At the end of the Assessment Phase the ‘Main Gate’ review represents the main investment decision on a programme and is the point at which a preferred procurement option/supplier is generally chosen. Depending on the value of the contract, the IPT Leader, in conjunction with the appropriate

²⁸ The structure of the IAB is the same as the EAC as outlined in section I (C), although its remit has been expanded to include responsibility for the scrutiny and approvals processes for all investment decisions across the Department.

²⁹ Evolution of the URD and SRD is mainly the consequence of advancements in technology.

DEC would present the IPT's business case and recommendation to the IAB. Programmes above £400 million, designated as Category A projects, require approval firstly by the IAB and then the ministerial Defence and Overseas Planning (DOP) Committee of the Cabinet Office. The DOP is entitled to question the IAB over its recommendations and to ask for a re-assessment if it is deemed necessary.³⁰ Projects with a value lower than £400 million³¹ are generally approved below IAB level although they can be passed to the IAB, and potentially the DOP, for approval if they are considered controversial or if no clear recommendation has been made.

- **Demonstration Phase** – Work to eliminate development risk in order to meet performance targets for manufacture is the focus of this stage in the procurement cycle. The selection of a single preferred supplier for a programme is not uncommon at this point. Contracts for manufacture are signed.
- **Manufacture Phase** – Production is undertaken in order to deliver the capability to the military requirement set out in the SRD and URD and within the time and cost parameters identified. The project IPT transfers to the DLO at this stage.

The National Audit Office's latest assessment of the success of Smart Acquisition is set out in its *Major Projects Report 2002*. Overall the report concluded:

There is a continuing improvement in project performance, especially regarding cost control, but maintaining this improvement will be the challenge. Notably, there are encouraging indications that Smart Acquisition is resulting in innovation in the design of programmes to deliver equipment capabilities faster, cheaper and better. Messages on the management of individual programmes to time and cost once they are underway are more varied.³²

More specifically it stated:

Overall costs are within approval, but time variation exceeds approval:

- Under the new approval process, total forecast costs are within total approved costs and have fallen again in-year.
- Slippage continues to be a problem, primarily on legacy projects.

There is a continuing improvement in performance:

³⁰ The Defence and Overseas Policy Committee consists of the Prime Minister (Chair), the Deputy Prime Minister, the Chancellor of the Exchequer, the Foreign Secretary, the Secretary of State for Defence, The Secretary of State for Trade and Industry and the Secretary of State for International Development.

³¹ Programmes between £100m-£400m are designated Category B; programmes between £20m-£100m are designated Category C; and programmes under £20m are designated Category D.

³² National Audit Office, *Ministry of Defence: Major Projects Report 2002*, HC91, 4 December 2002, p.1

- The Department is forecasting that it will meet 98 per cent of the Key User Requirements.
- Cost and time: performance across the majority of factors responsible for variation has improved.

Maintaining improved performance is now the challenge:

- Fourteen of the twenty projects are showing an adverse movement in-year.
- The Major Projects Report 2002 population includes a significant number of projects still in the early stages of their procurement cycle.
- There have been further developments within the Major Projects Report 2002 projects outside the reporting period.³³

Sir John Bourn, head of the NAO, said as the report was published:

The Ministry of Defence is controlling costs and expects to meet the technical requirements of the armed forces in most cases. But delays continue to be a problem with some projects. The reasons for these delays are complicated – a mixture of over-optimism and systemic factors. The Ministry of Defence has made some progress in tackling these factors this year, and future Major Project Reports will provide evidence to assess further progress.³⁴

The Defence Select Committee concluded in its report on *Defence Procurement* in July 2003:

Slippage continues to be a problem, particularly on older ‘legacy’ projects. But even in regard to newer projects which should be able to be fully moulded according to Smart Acquisition principles, there remains a question about the agility of the Department’s procurement systems.³⁵

The committee also went on to comment:

We are impressed with Sir Peter Spencer’s determination, as the new Chief of Defence Procurement, to make Smart Acquisition truly agile and responsive to equipment customer’s needs. He appears to share the view of the Chairman of the Defence Industries Council, and our own, that “we need to be prepared periodically to refresh Smart Procurement”.³⁶

In a report in March 2002 the National Audit Office also examined the success of the IPT concept in improving defence equipment acquisition. The NAO concluded that the IPTs

³³ *ibid*, p.4

³⁴ National Audit Office Press Release. Available online at: <http://www.nao.gov.uk/pn/02-03/020391.htm>

³⁵ Defence Select Committee, *Defence Procurement*, HC694, 23 July 2003

³⁶ *ibid*

had been introduced rapidly and successfully but needed to evolve further. It recommended that firm direction was required from the MOD to maintain the momentum behind the implementation of the teams and to ensure that they are successful in improving acquisition performance. The report recommended that the MOD should conduct a stocktake of its existing IPT structure to ensure that it reflected the experience gained to date and provided the most effective structure to deliver the benefits anticipated from Smart Acquisition.³⁷

Sir John Bourn commented:

The Department has made a quick and encouraging start to introducing IPTs and now needs to press ahead quickly with action to embed and drive forward the changes under the direction of the new Director General Smart Acquisition. My report makes a number of positive recommendations to help with this and I will be undertaking further work in the future to examine how successful IPTs are being in enabling a through-life approach to acquisition and improving performance.³⁸

B. Public-Private Partnerships (PPP)

PPP is a key element of the Government's approach to providing and modernising services in the public sector. Initiatives such as PFI, partnering and outsourcing are at the heart of the PPP concept and under Smart Acquisition the MOD has fully endorsed the use of these tools for providing services throughout the Department.

The MOD's policy paper on *Defence Acquisition* described the Department's approach to PPP as follows:

The MOD selects PPP projects on their merits. It employs PPP tools such as the Private Finance Initiative (PFI) and Partnering where they offer the potential to achieve greater value for money than could be achieved under more traditional ways of doing business, while improving or sustaining front-line capability. The MOD has no dogmatic preference for private over public, or vice versa.³⁹

1. Private Finance Initiative (PFI)

All equipment procurement programmes under Smart Acquisition are considered at the outset for their viability as a PFI. The MOD's own capital funding resources are used

³⁷ National Audit Office, *Ministry of Defence: Implementation of Integrated Project Teams*, HC671, 14 March 2002

³⁸ NAO Press Notice 24/02, 14 March 2002.

³⁹ Ministry of Defence, *Defence Acquisition*, December 2001

only when “PFI has been demonstrated to be unworkable, inappropriate or uneconomic”.⁴⁰

The *Defence Acquisition* policy paper stated:

In PFI, the Department contracts for services rather than assets, so the MOD first needs to decide whether it would be practical to meet its requirements by means of a contract under which services are provided rather than by the outright purchase of assets such as buildings and equipment. If so, the Department next considers whether such an approach has the potential to offer better value for money than if it bought assets directly. PFI aims to achieve this by allowing the MOD to focus on its core military tasks supported by a private sector partner, who can offer services more efficiently or at less cost because it is able to do things that the MOD cannot. For example, a contractor may be able to reduce the cost of providing a service if he is able to sell on spare capacity as an asset to other users.⁴¹

A key feature of PFI is that it offers the MOD greater potential for transferring risk to the private sector, while benefiting from additional capital investment. It also offers the private sector the opportunity to demonstrate innovation in its procurement solutions and provides the incentive to deliver the service to time, cost and performance targets. The scope for generating third party revenue is a key determinant in identifying the potential of a project for PFI.

The MOD’s PFI programme includes service accommodation, housing, information systems, utilities, training facilities and equipment. By 1 September 2003 fifty PFI contracts had been signed by the MOD.⁴² High profile projects have included the refurbishment of MOD Main Building in Whitehall and the construction of the Joint Services Command and Staff College at Shrivenham. From an equipment perspective the Roll-on Roll-off Ferries programme has been delivered under PFI; the satellite communications programme Skynet 5 and the Heavy Equipment Transport (HET) are currently underway under PFI. A number of other programmes including the Future Strategic Tanker Aircraft (FSTA) are currently intended to be procured under these arrangements.

The MOD’s *Acquisition Handbook* noted:

PFI is demanding but has realised savings of up to forty percent in forecast costs compared with other forms of procurement.⁴³

⁴⁰ Ministry of Defence, *The Acquisition Handbook*, 4th Edition, January 2002, p.22

⁴¹ *Defence Acquisition*, MOD Policy Paper No 4, p12, December 2001.

⁴² The MOD database of PFI projects, at September 2003, is available online at: http://www.mod.uk/linked_files/business/rptprojectsinternetsept03.pdf

⁴³ Ministry of Defence, *The Acquisition Handbook*, 4th Edition, January 2002, p.23

Professor Keith Hartley from the Centre for Defence Economics at the University of York commented on the viability of PFI in defence:

Governments can always borrow more cheaply than the private sector. If PFI/PPP contracts are to lead to genuine cost savings, the extra financing costs for the private sector must be offset by savings elsewhere on the project (eg. management and running costs over the life of the project).⁴⁴

Some analysts have suggested, however, that the provision of front-line equipment would be the real test of how far PFI meets the MOD's needs. Alex Nicoll, writing in the *Financial Times* in December 2001, said:

...although many PFI projects are under way in the MOD, actual progress in converting MOD procurement to PFI is slow. Since the FT's PFI survey was last published a year ago, just three new contracts have been signed, and they are of a similar nature to many of the 34 previous deals signed since 1996. Many projects involve outsourcing of training and associated equipment; accommodation for service personnel; and provision of civil services such as cars, trucks and water...It is front-line projects such as the tanker [aircraft refuelling], however, that will really determine to what extent the MOD's particular needs can be met through PFI.⁴⁵

The Defence Select Committee warned in its report on *The MOD's Annual Reporting Cycle 2000-01* of the implications of undertaking PFI arrangements for front-line capabilities:

We welcome the assurance that PFIs will not compromise front line military capability but we detect a shift in the policy on the boundaries of PFIs since the SDR less than three years ago. We note that some existing programmes – for example, the Future Strategic Tanker Aircraft – are already very close to that front line. We repeat our earlier warning about the dangers of allowing PFI to take control of its war fighting capabilities out of the MOD's hands.⁴⁶

In its report on *Major Procurement Projects* in July 2002 the Committee reiterated its concerns over the use of PFI in the front line:

Whether PFI delivers value for money should depend not just on a purely financial balance of costs and benefits, but also on whether risk is managed more efficiently. In the defence field, getting the balance of risks wrong does not just undermine the calculation of the cost-benefit of particular projects; it can have profound consequences for the operational readiness and effectiveness of our Armed Forces, and ultimately for the safety of our Service personnel operating in

⁴⁴ Professor Keith Hartley, "Military outsourcing: UK experience", *Centre for Defence Economics*, University of York

⁴⁵ *Financial Times*, 3 December 2001.

⁴⁶ Defence Select Committee, *The MOD's Annual Reporting Cycle 2000-01*, HC144, 2 May 2001, p.xii

hostile environments. It is in that context [...] that we remain concerned about the lack of clarity in the use of PFI, particularly its further encroachment into front-line areas. These risks are present in several of the projects that we have examine in this inquiry and are perhaps most glaring in the case of the Future Strategic Tanker Aircraft.⁴⁷

In response to these concerns the MOD clarified its position on using PFI for front-line capabilities in a Supplementary Memorandum to the Committee:

The use of PFI is considered on a case-by-case basis. Ministerial guidance is that PFI should be used only where it is appropriate, workable and economic. Detailed criteria have been developed in order to assess these objectives, one of which is operational effectiveness. In respect of operational effectiveness, issues such as operational flexibility and loss of core skills will be taken into account. This work is done in the feasibility stage and can even result in projects that “do not move” being rejected for PFI because of the unacceptable operational impact if that project were to be a PFI... The public sector comparator is not the sole means of determining value for money. Other factors, particularly the quality of services, are also taken into account as part of the assessment and appraisal processes.⁴⁸

2. Partnering

The MOD’s *Acquisition Handbook* describes partnering as:

The development of new, much more co-operative long term relationships between the MOD and industry. Partnering differs from conventional contracting relationships in that effective communication strategies amongst partners lead to trust, better and earlier identification and hence management of project risks, and increasing better value for money being gained in large scale complex requirements.⁴⁹

The most prominent example of a partnering arrangement established to deliver frontline capability is on the Future Carrier (CVF) programme. On 30 January 2003 the MOD announced that an industrial alliance between the MOD and various industrial partners, including BAE Systems as prime contractor and Thales UK as a key supplier, would be established to deliver the CVF project.

In a Statement to the House the Secretary of State for Defence, Geoff Hoon, outlined:

Our detailed analysis shows that each company has significant strengths. BAE Systems has displayed a sound understanding of the project's complexities in its project management and prime contracting, and has developed a good

⁴⁷ Defence Select Committee, *Major Procurement Projects*, HC779, 10 July 2002

⁴⁸ *ibid*, Appendix 25

⁴⁹ Ministry of Defence, *The Acquisition Handbook*, 4th Edition, January 2002, p.25

relationship with all the key shipyards. It also demonstrated the skills that are necessary to integrate the different systems into an effective warship. Thales UK has provided an innovative design that is flexible enough to meet our needs. It has strengths in a number of key areas, including in weapon and defence systems and the interface between the ship, aircraft and flight deck operations.

We have therefore decided that, to deliver value for money and provide the best capability, it is important and, indeed, sensible to exploit all those strengths. We judge that a partnership appears to offer the best means of drawing in the necessary resources and expertise to deliver a programme of such magnitude. We envisage that this alliance will be led by BAE Systems as the preferred prime contractor, with responsibility for project and shipbuilding management. Thales UK will assume a major role as the key supplier of the whole ship design. We foresee that the Ministry of Defence will also take up a formal role in the alliance for those parts of the programme for which we are rightly responsible. That would involve the management of appropriate risk and contingencies and the provision of assets such as suitably trained manpower and the JSF aircraft.

This innovative approach builds on the principles of smart acquisition and the defence industrial policy that was published last October. It will enable us to make the most of the resources and strengths of both companies and the skills and expertise of the Ministry of Defence project team.

Both BAE Systems and Thales UK have indicated their willingness in principle to participate in such an alliance. The approach will be based on proper customer and supplier relationships, working collaboratively to achieve challenging targets. It will be underpinned by a robust contractual arrangement. Risk will be allocated to the party best suited to manage and mitigate that risk and the rewards will be shared so that it is in the interests of all parties for the programme to succeed. Further work will be required with both companies to establish the detailed contractual arrangements.

Subject to reaching a satisfactory outcome to these negotiations, and with subsequent confidence that the alliance is operating effectively during the final part of the assessment phase, we intend to reach the final investment decision in spring 2004. At that stage, we will place the prime contract and permit the alliance to move into the demonstration and manufacture phase, when the ships will actually be built. We remain fully committed to achieving our declared in-service dates for both ships in 2012 and 2015 respectively.⁵⁰

Commenting on the announcement the Shadow Defence Secretary, Bernard Jenkin, stated:

this is not so much a decision as a fudge. The addition of two full-sized aircraft carriers to the Royal Navy's fleet, along with the introduction of the new joint

⁵⁰ HC Deb 30 January 2003, c1027-8

strike fighter, will represent a huge increase in Britain's ability to project, sustain and protect military force anywhere in the world. So we welcome any progress towards the launch of the new ships, but we fear that this programme is now beset by uncertainty [...]

the Secretary of State describes his announcement as "innovative", but he is being a little modest. He has not so much announced a decision as the start of a whole new process: the formation of an as yet ill-defined alliance that is entirely unformed and agreed only "in principle". He remains committed to the in-service dates of 2012 and 2015—dates that are long after he is likely to have departed—but if in a year's time his proposed alliance is judged not to be operating successfully, as he put it, where will that leave the Government's programme? The so-called smart procurement policy was meant to avoid the vexed issue of work sharing. This project started out as a clear competition, but has not the Secretary of State bottled out in the past few weeks by unexpectedly deciding to split the work between the two main competitors?⁵¹

The Liberal Democrat Spokesman, Paul Keetch, commented:

Can the Secretary of State confirm—yes or no—that the recommendation from the Defence Procurement Agency was for a single prime contractor? Does not a single contractor represent a single point of control? Who will really run the project? Will it really be BAE Systems? Who will own the rights to the design of the future carrier: BAE or Thales? Can the right hon. Gentleman give a single example of an alliance producing a contract on time and on budget? In short, after a three-year contest, why have the Government decided on such an alliance? If it is such a good idea, why was it not decided on at the start of the contract?

The Liberal Democrats believe that the future carrier programme is essential to our British military future, and we congratulate the Government on fulfilling their obligations under the strategic defence review. I hope that the alliance will work, but it will be for the Secretary of State to demonstrate that that design does not become one of our major overruns.⁵²

An article in *Jane's Defence Weekly* in April 2003 summed up concerns over the CVF project:

[in February 2003] executives from both companies [BAE Systems and Thales] expressed fears that this 'shotgun marriage' could prove difficult to consummate, given that the design concepts, build strategies and prime contracting methodologies proposed by BAE Systems and Thales were so significantly different. This in turn, they said, threatened the delivery of the programme to cost, time and capability.

⁵¹ HC Deb 30 January 2003, c1028-9

⁵² HC Deb 30 January 2003, c1031

Negotiations on the formation of the CVF alliance have been continuing since the beginning of February. Industry and MOD officials acknowledge that their successful conclusion is a matter of some urgency so that work can be taken forward to support a Main Gate submission currently planned for August [...]

The complexities of striking a deal to establish the alliance are prompting concerns that the current timetable to Main Gate may prove unachievable. There are also worries over the additional risk margins being costed into the programme by BAE Systems which, as prime contractor, is being asked to deliver a design it did not develop.⁵³

C. International Collaboration

The SDR highlighted the importance of international collaboration to the UK equipment procurement programme. It stated that international collaboration:

offers tangible military, economic and industrial benefits and it is essential that the UK remains at the forefront of developments in this area of joint endeavour.⁵⁴

Under Smart Acquisition the application of “Smart Procurement” techniques to collaborative programmes is regarded as essential, as time, cost and performance risks in such projects are significantly increased.

Collaborative programmes involving the UK have been regarded by many analysts as having had mixed success to date; mainly due to a lack of funding, a divergence of national interests and requirements, and disputes over industrial participation. For example, in 1999 the UK withdrew from the Horizon frigate programme, while in July 2003 the UK also pulled out of the tri-national Multi-Role Armoured Vehicle (MRAV) in favour of the forthcoming Future Rapid Effects System (FRES). The A400M transport aircraft and the Meteor missile programme have also suffered significant delays mainly due to funding issues in a number of the partner nations.

Progress on the collaborative European Technology Acquisition Programme (ETAP), which was established in November 2001, has also been mixed. ETAP aims to assess the development of collaborative technology related to combat air systems over the next twenty years. In a Written Answer on 23 July 2002 the then Parliamentary Under Secretary of State for Defence, Dr Lewis Moonie, outlined the UK’s position with respect to this initiative:

The European technology acquisition programme (ETAP) is about collaborative technology development related to combat air systems rather than procurement of

⁵³ “Worries grow that UK carrier project will slip”, *Jane’s Defence Weekly*, 23 April 2003

⁵⁴ Ministry of Defence, *Strategic Defence Review: Supporting Essays*, July 1998, Essay Ten

specific equipments. United Kingdom decisions on technology development within ETAP will reflect the key capabilities required of the UK's future offensive air system. If one or more of our ETAP partners identify the same technology area as a priority, we will jointly decide whether a collaborative ETAP technology demonstration programme with European industry represents best value for money.⁵⁵

However the UK's involvement with other European nations in the Joint Strike Fighter (JSF) project has cast doubt over the long-term viability of ETAP. The UK has been a full collaborative partner with the US in the Concept and Demonstration phase of the JSF since 1996, and in January 2001 signed a Memorandum of Understanding with the US for continued participation as a full partner in the Engineering and Manufacturing Development phase.

The Ministry of Defence commented in a press release:

Participation in the JSF programme represents a tremendous opportunity for UK industry. UK companies are well represented in each of the competing consortia. We expect that work on the EMD phase will create or sustain 5,000 UK jobs in around 70 companies.

JSF will play a crucial part in continuing our transatlantic partnership, maintaining NATO interoperability and improving European military capability [...]

The cost to the UK of the EMD phase will be in the order of £1.3 Billion, plus some further £600 Million to fund work on UK-specific requirements. Including export orders, the JSF production run may approach 5000 aircraft, estimated to be worth some \$400 Billion through life. JSF may well be the largest ever military procurement programme. Contracts are expected to be awarded for this phase of the programme later this year.⁵⁶

The JSF is intended as a replacement for the UK's land-based Harrier and Sea Harrier aircraft and would fulfil the UK's Future Joint Combat Aircraft (FJCA) requirement. In September 2002 the MOD also announced that up to 150 Short Take-off and Vertical Landing (STOVL) variants of the JSF (F35) would be procured to equip the Future Carrier (CVF). Lockheed Martin was selected as the prime contractor for the JSF programme in October 2001.

The UK has participated within a number of international collaborative frameworks over the last decade aimed at encouraging and streamlining multinational procurement and developing capabilities. Among those the Organisation Conjointe de Coopération en Matière d'Armement (OCCAR), the NATO Defence Capabilities Initiative/Prague

⁵⁵ HC Deb 23 July 2002, c904W

⁵⁶ Ministry of Defence Press Release, 004/01, 17 January 2001

Capabilities Commitment (DCI/PCC) and the European Capabilities Action Plan (ECAP) have made the most progress.⁵⁷ The Six-Nation Framework Agreement and the UK/US Declaration of Principles have also been significant.

1. Organisation Conjointe de Coopération en Matière d'Armement (OCCAR)

OCCAR was established by the UK, France, Germany and Italy in November 1996 in a bid to provide more effective and efficient arrangements for the management of collaborative procurement programmes between the four nations. The OCCAR Convention, which conferred legal status on the organisation, was ratified by all member states in 2000-01 and came into force on 28 January 2001.⁵⁸

Under the Convention the organisation is able to place and manage contracts in support of programmes placed within its remit, and to employ its own staff. It also gives a legal basis to the Founding Principles which, among other things, require OCCAR Member States to renounce the principle of *juste retour* which calls for national workshare in a programme to be allocated on the basis of cost contribution. Harmonisation of future military requirements is stated as a long term objective of the organisation.

Contrary to popular belief, OCCAR is not a procurement agency, as it does not take procurement decisions on behalf of its members. Multinational programmes are placed under the management of the organisation at the discretion of the partner nations involved in the project. The most recent example is the A400M transport aircraft project, which came under OCCAR management in May 2003.

Under the founding principles of OCCAR, membership of the organisation is open to other European nations, subject to their involvement in a collaborative equipment programme involving at least one OCCAR partner, and their acceptance of the Founding Principles and ratification of the Convention. On the basis of the A400M programme Belgium, Spain and The Netherlands have applied to join. The remaining partner nations in the A400M project have been designated as Participating States. There is no obligation for them to join OCCAR.

Other programmes under the management of OCCAR are the Tiger helicopter; Roland surface-to-air missile; Boxer armoured vehicle (designated in the UK as the Multi-Role Armoured Vehicle); COBRA long-range battlefield radar; MILAN anti-tank missile; and the FSAF family of surface-to-air anti-missile systems. The inclusion of the Principle Anti-Air Missile (PAAMS) project between the UK, France and Italy as part of FSAF is currently under consideration. PAAMS will be the principal missile capability deployed on the UK's Type 45 destroyer.

⁵⁷ The UK has also participated in the Western European Armaments Group and the Western European Armaments Organisation.

⁵⁸ A copy of the Convention is available online at:
<http://www.occar-ea.org/C1256B0E0052F1AC/vwContentFrame/N254SMVV967SLEREN>

The SDR highlighted the importance of OCCAR to the UK's pursuit of smart procurement:

British membership of... OCCAR, the quadrilateral armament structure with France, Germany and Italy, presents a real opportunity to establish with our major European partners improved collaborative practices which deliver value for money products able to compete effectively in world markets. Our work on 'Smart Procurement' would be beneficial to such a process. We remain fully committed to the pursuit of common OCCAR objectives...⁵⁹

According to many analysts the integration of SPI techniques into OCCAR best practice has been evident in the last few years. In its *Acquisition Handbook* of January 2002 the MOD commented:

Several of the UK's major partners are starting to think along Smart Acquisition lines, and this trend is also evident in the OCCAR framework. The aim is that the introduction of Smart Acquisition principles into collaborative projects will reverse the trend of magnified risks in favour of better-managed collaborative programmes.

DPA and DLO staff have been closely involved in the development of rules and procedures for the management of collaborative defence equipment projects by OCCAR [...] As a result, many Smart Acquisition concepts have been adopted for use by the organisation, including the use of integrated project teams and a through-life approach to acquisition. Work is also underway to develop simplified and harmonised approvals processes for OCCAR-managed programmes.⁶⁰

The future of the OCCAR organisation, which has been regarded by some as the precursor to a fully fledged European armaments agency, is currently the subject of debate among analysts, in light of the current proposals under Article III-207 of the EU Draft Constitution for the establishment of a European Armaments, Research and Military Capabilities Agency. Under the authority of the Council, the agency would:

- Evaluate the progress made by each Member State in fulfilling its capability commitments;
- Promote the harmonisation of operational requirements and put forward measures to satisfy those requirements, including compatible procurement methods and multilateral projects. Multinational projects would be managed by the agency and specific groups would be set up to bring together Member States involved in those joint projects;

⁵⁹ Ministry of Defence, *Strategic Defence Review: Supporting Essays*, July 1998, Essay Ten.

⁶⁰ Ministry of Defence, *The Acquisition Handbook*, 4th Edition, January 2002, p.21

- Support defence technology research and plan and coordinate joint research activities to meet future operational needs;
- Contribute to the strengthening of the defence industrial and technological base;
- Identify measures to improve the effectiveness of defence spending.

Unlike OCCAR, membership of the agency would be automatically available to any Member State wishing to participate. The statute, the location and the operational rules of the agency would be decided by QMV in the Council of Ministers.⁶¹

Francis Gevers has argued in an article in *Jane's Defence Weekly* that:

Within the framework of [...] organisations such as OCCAR, the Organisation for Joint Armament Co-operation, nations have retained the right to handle any tasks themselves or to go international when national solutions are impossible, turning the international body into an expensive shell. Two reasons can be identified for this unfortunate situation. First, going international implies a partial loss of national decision powers, as each decision will have to take the wishes of other nations into consideration. And secondly, transfer of a responsibility to an international body will result in the loss of work and status for the national bodies that would normally have performed the task. These two elements may well influence the forthcoming political decisions [...]

Any new armaments agency will only be successful if it receives executive powers it needs and if the real tasks are relinquished by national governments.⁶²

The Lords European Union Select Committee suggested in its report on the external action articles of the Draft Constitution that:

Such an Agency might well help to improve the capabilities of the armed forces of Member States, but care needs to be taken to ensure that it does not become a tool for protectionism or constrain the ability of Member States to order armaments independently.⁶³

2. NATO/ EU Initiatives

With the exception of the NATO Airborne Early Warning and Control aircraft (AWACS), assets designated to NATO and EU-led operations are nationally owned. However, the disparity in defence spending between the US and its European allies since the end of the Cold War, particularly in procurement and research and development (R&D), has created a gap in capabilities. Some analysts believe this has also created a

⁶¹ European Draft constitution, article III-207

⁶² "Europe's future armaments agency: is it doomed to repeat the past", *Jane's Defence Weekly*, 10 September 2003

⁶³ Lords Select Committee on the European Union *The Future of Europe: Constitutional Treaty – Draft Articles on External Action* HL Paper 107 2002-03 13 May 2003 p.13

credibility crisis, both for the Alliance and for EU efforts to establish a defence capability through the European Security and Defence Policy (ESDP). The US currently spends close to 3.5% of GDP on defence, while European Member States spend, on average, only 2%. Within Europe there are also disparities. Germany spent 1.5% of GDP on defence in 2002, whereas both the UK and France increased their defence budgets during the same year. Under the UK Government Spending Review in July 2002 an additional £3.453 billion over three years was allocated to the defence budget.⁶⁴ In September 2002 the French Military Programme Bill for 2003-2008 allocated an average of €14.64 billion (approximately £9.63 billion) to equipment appropriations, which constituted a rise of approximately 12.4% between 2002 and 2003, and 7.5% between 2003 and 2004.⁶⁵

However, as an article in *The Sunday Times* commented:

Gerhard Schröder, the German Chancellor, made it clear that his country's parlous economic state meant that there could be no increase in military spending this year or next. Other countries, such as the Netherlands and Italy, are equally reluctant to spend more, citing constraints on borrowing under EU rules on the single currency.⁶⁶

Since 1999 NATO and the EU have launched capability procurement initiatives to address equipment shortfalls and identify potential areas for collaborative procurement. In its "Food for Thought" Paper, presented to a meeting of EU officials in Rome on 29 August 2003, the UK highlighted the importance of these initiatives. The paper outlined five priorities for the UK including:

Closing the key capabilities gap in the Headline Catalogue (securing new commitments; monitoring progress against an agreed timetable) [...]

Multi-national cooperation (encouraging member states to work together on a voluntary basis, including under the auspices of the [European Capabilities] Agency, to increase their capabilities in shortfall areas. The priority must be the ECAP and PCC initiatives [...])

Capabilities (taking forward and establishing the Agency, with the necessary focus [on it being] "capabilities driven").⁶⁷

a. *NATO Defence Capabilities Initiative/ Prague Capabilities Commitment*

NATO launched its Defence Capabilities Initiative (DCI) at the Washington Heads of State and Government Summit in 1999. The aim of the DCI was to pursue capability

⁶⁴ Ministry of Defence Press Release, 15 July 2002

⁶⁵ French Ministry of Defence, *Military Programme Bill of Law 2003-2008*. This is available online at: <http://www.defense.gouv.fr/english/files/d140/index.htm>

⁶⁶ "America dwarfs new recruits", *The Sunday Times*, 24 November 2002

⁶⁷ Foreign and Commonwealth Office Memorandum, *Food for Thought Policy Paper*, 29 August 2003

improvements, both nationally and jointly. NATO Secretary General Lord Robertson stated at the time:

The Defence Capabilities Initiative is designed to ensure that all Allies not only remain interoperable, but that they also improve and update their capabilities to face the new security challenges.⁶⁸

Much of the focus of the DCI had been on lessening the capability gap in areas of key strategic importance such as C4ISTAR,⁶⁹ strategic lift, precision guided munitions and the suppression of enemy air defences. In order to avoid duplication and overlap, the DCI was also closely tied to progress made by EU members on the Helsinki Headline Goal and the establishment of the European Rapid Reaction Force (ERRF).⁷⁰

The Defence Select Committee report on *The Future of NATO* of July 2002 commented:

NATO carried out an assessment of progress in implementing the DCI for the NAC meeting of defence ministers in June 2001, which concluded that: 'Although progress has been made in certain areas, further efforts are required to achieve the necessary improvement.' 'Critical and long standing deficiencies' remained in such areas as: suppression of enemy air defence and support jamming; combat identification; intelligence, surveillance and target acquisition; day/night and all weather air weapons systems; all aspects of air defence, and capabilities against nuclear, biological and chemical weapons.⁷¹

Guillaume Parmentier in his article, "Rejuvenating the Alliance", in the Summer 2002 edition of *NATO Review* also argued:

A key lesson needs to be drawn from experience gained in implementing the Defence Capabilities Initiative...setting too many priorities means that there are effectively no priorities. The 58 items identified for priority action diluted the focus of the DCI, making it too easy for nations to find excuses for not coming up with the essential goods.⁷²

In light of criticisms of the progress made with the DCI, and the need to re-address NATO's military capabilities in the post-11 September 2001 environment, work towards a new DCI concept was begun in June 2002.

⁶⁸ NATO Fact Sheet *NATO's Defence Capabilities Initiative*, 9 August 2000. Available online at <http://www.nato.int/docu/facts/2000/nato-dci.htm>

⁶⁹ C4ISTAR stands for: command, control, communications, computers, intelligence, surveillance, target acquisition and reconnaissance.

⁷⁰ Further information on the Helsinki Headline Goal is available in Library Research Paper RP00/84 *Common European Security and Defence Policy: A Progress Report*.

⁷¹ Defence Select Committee *The Future of NATO*, HC 914 24 July 2002, p.49

⁷² Guillaume Parmentier "Rejuvenating the Alliance" *NATO Review*, Summer 2002

As Dr Jamie Shea, Director of Information and Press for NATO, pointed out in an interview with the British American Security Information Council (BASIC) in April 2002:

11 September brings back to us an old problem in NATO which has not gone away, but which requires urgent treatment: the question of defence capabilities...we have seen the United States pull ahead spending \$48bn more than NATO, China and Russia combined. The danger is that there will be a kind of unbridgeable chasm between the Americans and the Europeans, which will make coalition operations more difficult. We won't be able to communicate, we won't be interoperable...The Europeans spend \$150m a year, which was about half of the US defense budget prior to 11 September, but it is calculated that they only get 10-12% of what the Americans get in terms of output.⁷³

Consequently, the NATO Defence Ministers meeting on 6 June 2002 concluded:

A greater and more focused effort is now necessary. We therefore directed the Council in Permanent Session to prepare recommendations for a new capabilities initiative, taking into account military advice and national proposals. This should focus upon a small number of capabilities essential to the full range of Alliance missions.⁷⁴

Four priorities for the new DCI were established:

- To defend against chemical, biological, radiological and nuclear attacks.
- To ensure secure command communications and information superiority.
- To improve interoperability of deployed forces and key aspects of combat effectiveness.
- To ensure rapid deployment and the ability to sustain combat forces.⁷⁵

The new initiative would also be based on national commitments with specific milestones and target dates, a marked difference from the previous DCI. The intention would be to provide the impetus for members to re-prioritise defence spending, reduce force numbers, shift resources towards the upgrading of equipment, and co-operate on a multinational level where possible, including, in some cases, the pooling of resources and role specialisation. A system of high-level monitoring was expected to be put in place.

In order to avoid the duplication of resources, the DCI would also continue to work in tandem with the European Capability Action Plan (ECAP), devised under the auspices of the EU, and its attempts to develop a rapid reaction capability (see Section II C).

⁷³ "NATO Obviously has to move ahead" *BASIC Newsletter on International Security*, April 2002

⁷⁴ NATO Press Release *Statement on Capabilities*, 6 June 2002. Available online at <http://www.nato.int/docu/pr/2002/p02-074e.htm>

⁷⁵ *ibid*

At an informal meeting of NATO defence ministers in Warsaw on 24-25 September 2002, proposals aimed at enhancing the Alliance's military capabilities, and specifically those identified in the four key areas, were reviewed. A set of commitments and programmes were put forward for discussion and adoption at the Prague Summit in November 2002.

The Prague Capabilities Commitment (PCC) was adopted at Prague as the successor to the DCI. Although one of the more high profile decisions of the summit, the declaration on the PCC was largely symbolic, with the parameters for the commitment having been laid down in June 2002. Focusing on the four priorities identified in June 2002 by NATO Defence Ministers, the PCC attempted to establish a roadmap towards creating niches of excellence rather than attempting to sustain interoperability across the whole combat spectrum.

The *Prague Summit Declaration* stated:

Individual Allies have made firm and specific political commitments to improve their capabilities in the areas of chemical, biological, radiological, and nuclear defence; intelligence, surveillance and target acquisition; air-to-ground surveillance; command, control and communications; combat effectiveness, including precision guided munitions and suppression of enemy air defences; strategic air and sea lift; air-to-air refuelling; and deployable combat support and combat service support units.⁷⁶

The Declaration went on to state:

Our efforts to improve capabilities through the PCC and those of the European Union to enhance European capabilities through the European Capabilities Action Plan should be mutually reinforcing, while respecting the autonomy of both organizations, and in a spirit of openness.

We will implement all aspects of our Prague Capabilities Commitment as quickly as possible. We will take necessary steps to improve capabilities in the identified areas of continuing capability shortfalls. Such steps could include multinational efforts, role specialisation and reprioritisation, noting that in many cases additional financial resources will be required, subject as appropriate to parliamentary approval. We are committed to pursuing vigorously capability improvements. We have directed the Council in Permanent Session to report on implementation to [NATO] Defence Ministers.⁷⁷

⁷⁶ Prague Summit Declaration issued by NATO Heads of State and Government, 21 November 2002. A full copy of the declaration is available online at: <http://www.nato.int/docu/pr/2002/p02-127e.htm>

⁷⁷ *ibid*

A number of multinational efforts aimed at procuring key strategic assets have been established.

A press release issued by the Bush administration on 21 November 2002 stated:

- Germany is committing to lease C-17 transport aircraft as an interim measure, and lead a consortium of nations aimed at pooling airlift resources and capabilities.
- Canada, France, Italy, the Netherlands, Spain and Turkey are individually committing to buy UAVs.
- The Netherlands is leading a consortium with Canada, Denmark, Belgium and Norway to pool purchases of precision-guided munitions (PGMs).
- Spain and the Netherlands are buying munitions for suppression of enemy air defences (SEAD).
- Denmark and Norway are contributing to air-to-air refuelling and Spain is leading a consortium of nations interested in pooling their refuelling capabilities.
- Norway and Germany have committed to improving maritime counter-mine capabilities.
- Poland and Hungary are improving nuclear, chemical, and biological identification and defence capabilities.⁷⁸

An article in *Jane's Defence Weekly* provided further detail on some of these capabilities:

Strategic Lift: Germany is organising an effort to lease between eight and 15 “outsized aircraft” such as Boeing C17s or Antonov An-124s to bridge the gap until 2008 when the European-built Airbus Military A400M is expected to enter service. A NATO official said 12 allies are already committed in principle to a plan to create a NATO agency similar to the one that operates the NATO-owned fleet of E-3A Air Warning and Control System (AWACS) aircraft, except that the transports would be leased on a long-term basis.

Inflight refuelling: Spain is leading a plan to bridge another gap by securing some 48 tanker aircraft by 2005. The NATO official said so far 10 countries are involved and “there are good long-term prospects for all nations increasing their fleets of tankers” through leasing, refitting older aircraft and new purchases, including a special A400M tanker version that some nations, including Italy will buy.

PGMs: The Netherlands is looking to expand a programme involving five nations—Denmark, Greece, the Netherlands, Norway and Portugal—that wish to purchase PGMs for their F16 fighters. This is a unique problem since US export laws prohibit the sale of the most sophisticated armaments abroad. “The Dutch are talking to the US on this and the Americans are probably going to come up

⁷⁸ “NATO: Building new capabilities for new challenges”, *White House Press Release*, 21 November 2002

with something positive involving the same degree of accuracy as the US system”
a NATO official said...⁷⁹

In the week prior to the Prague Summit, the National Armaments Directors of France, Germany, Italy, the Netherlands, Spain and the United States also signed a Statement of Intent to assess co-operative development of a radar system that would be an essential element of an Alliance Ground Surveillance (AGS) capability.⁸⁰

In a speech to the Konrad Adenauer Stiftung on 12 December 2002 NATO Secretary General Lord Robertson commented on the achievements of Prague:

It is unacceptable that our countries spend hundreds of billions of euros on defence every year, but cannot deliver the military capabilities we need, when we need them. Over the years, various efforts to make improvements have been made, including within NATO. And they have delivered some results. But in the end, each initiative foundered on one of three shoals. Either the plan was unclear, or it did not have political support from the top, or it was deemed unaffordable.

At Prague we demonstrated that we had learned our lessons. NATO's 19 Heads of State and Government undertook to make major changes to Alliance capabilities...First, they made clear and precise commitments. Through what we call the Prague Capabilities Commitment, each and every NATO nation pledged to make specific improvements to the key military capabilities we need today, such as strategic air and sea lift, air refueling, and precision guided munitions. And these pledges came with specific timelines for development. Already a first.⁸¹

The commitment to capabilities made at Prague was a decisive step forward for the stalled Defence Capabilities Initiative and a demonstration of solidarity by NATO Member States towards underpinning previous rhetoric with practical action. However, to avoid the PCC and other initiatives becoming a symbolic gesture, it has been widely acknowledged that both Member States and Accession States must deliver on defence spending and, in the absence of expenditure increases, spend more effectively.

Robert Bell, NATO Assistant Secretary General for Defence Support, has suggested:

Success or failure in enhancing NATO's defence capabilities will...depend in great measure on the willingness of governments to invest more resources to acquire more defence capabilities, quickly and efficiently. It goes without saying

⁷⁹ “NATO's build-up to Prague”, *Jane's Defence Weekly*, 13 November 2002, p.27

⁸⁰ NATO Press Release, 21 November 2002

⁸¹ Speech by NATO Secretary General Lord Robertson to the Konrad Adenauer Stiftung on 12 December 2002

that the defence procurement community, and in particular the defence industry, will need to be able to react speedily to these requirements...To ensure the success of the Prague Capabilities Initiative, we need to have an understanding of what defence expenditures are really going to be made available. Otherwise, they risk the danger of the PCC becoming largely a theoretical, paper, exercise.⁸²

He also argued that:

One main reason for defence capability asymmetries as between the two sides of the Atlantic is the difference in the size of the defence input, which is growing. Europe's defence spending for some years has been running at about 60% that of the US, but its military research and development spending is only one quarter of the US level, and these ratios have not improved in Europe's favour, given the recent significant increase in the US defence budget...

Secondly, a fundamental question before the European and Canadian allies...is how they view their future military operational partnership with the United States. Do Europe and Canada wish to be a full partner of the United States across the full spectrum of transformational warfighting capabilities now associated with high-intensity conflicts?...and thus have forces which can join those of the US in high-intensity, high-tech, long-range coalition expeditionary operations? Or will Europe and Canada end up opting— perhaps by default— for far more modest (and less expensive) crisis management and peacekeeping tasks including post conflict reconstruction tasks? I hope the former will be the case.⁸³

b. European Capabilities Action Plan (ECAP)

The launch of the “Helsinki Headline Goal” at the Helsinki European Council in December 1999 represented a milestone in the work on a European Security and Defence Policy (ESDP). The Headline Goal laid plans for the establishment by the end of 2003 of a European Rapid Reaction Force (ERRF) of 60,000 personnel, with the ability to sustain itself in the field for one year.

In order to support the Helsinki proposals, a number of initiatives aimed at identifying EU military capabilities and assets were established. These culminated in the EU Capabilities Commitment Conference (CCC) on 20 November 2000. The CCC allowed EU Member States to voluntarily pledge military assets for use in any future deployment by the ERRF. It also allowed Member States to identify areas of capability shortfall.⁸⁴

Progress in implementing the objectives of the CCC was discussed at the EU Capabilities Improvement Conference (CIC) on 19-20 November 2001. One of the main conclusions

⁸² Robert Bell, “The Pursuit of Enhanced Defence Capabilities”, *NATO's Nations*, Edition 4/2002

⁸³ *ibid*

⁸⁴ Library Research Paper 01/50 *European Security and Defence Policy: Nice and Beyond*, provides some background to the Helsinki Headline Goal and the CCC.

of the CIC was for the establishment of the European Capabilities Action Plan (ECAP), which would draw Member States together in nineteen dedicated working groups focused on specific capability areas.

In order to avoid duplication between ECAP and NATO's DCI/PCC, mechanisms for co-ordination between the EU and NATO were put in place. One of the main channels for information sharing, thus far, has been through the European Security and Defence Identity (ESDI) initiative of the Atlantic Alliance.

Speaking at a meeting of the EU General Affairs Council (GAC) on 19 November 2002, the EU High Representative for the Common Foreign and Security Policy, Javier Solana, commented:

In many ways we can be satisfied of the progress made in European Security and Defence Policy (ESDP) over a short period of time. There is one area though where I think not enough has been made: the improvement of European military capabilities. We keep repeating that improving European military capabilities is at the core of the ESDP project and a fundamental condition for its success.⁸⁵

On ECAP more specifically, he stated:

The general approach of the European Capabilities Action Plan (ECAP) has paid off and proven its effectiveness in securing substantial participation of Member States. The interest and focus on military capabilities has definitely increased...The ECAP appears to be effective in generating viable options for resolving shortfalls or reduce them in a significant way...Active panels address most of the shortfalls apt to be remedied by ECAP. The majority of significant ones are under consideration...Co-operation with NATO has been effective from the outset. It is however, an area for further improvement.⁸⁶

However, he went on to comment:

We do not have a transparent overall picture of the state of play in the various panels. In these conditions it is difficult for Ministers of Defence to collectively assess progress and give meaningful political guidance for the way ahead...With a few notable exceptions, there are no significant increases in European defence budgets. This situation creates a serious problem of credibility.⁸⁷

In March 2003 the various ECAP panels submitted their conclusions on capability shortfalls and potential procurement options to an informal meeting of EU Defence Ministers.

⁸⁵ Intervention by Javier Solana, EU High Representative for the Common Foreign and Security Policy at the General Affairs Council, 19 November 2002

⁸⁶ *ibid*

⁸⁷ *ibid*

An article on *Agence Europe* outlined:

These panels have identified various kinds of short, medium and long-term solutions (procedural improvements and force training, the acquisition of new capabilities via leasing, in particular, and the sharing of databases), which must now be implemented by project groups. Pending the inter-ministerial conference on EU military capabilities during May, when a new catalogue of capabilities for 2003 will be established and the project groups will be designated, ministers will hold a first exchange of views on the solutions proposed by the boards.⁸⁸

On 19 May 2003 EU Defence Ministers adopted a *Declaration on EU Military Capabilities*. The Declaration stated:

9. Ministers welcomed the results of the first phase of the ECAP. All 19 activated Panels have delivered their final reports, bringing the ECAP process to a new, more challenging phase. Many Panels have articulated options to acquire additional capability both by procurement and non-procurement initiatives. The ECAP will now shift from the identification of these possible options to the establishment of Project Groups focussed on the implementation of concrete projects, including solutions through acquisition or other solutions such as leasing, multinationalisation and considering possibilities for role specialisation. In order to support the ECAP process Personal Representatives of the Ministers of Defence will continue to meet.

10. On the procurement side, the Project Groups are expected to provide plans and programmes to enable participating Member States to implement new capabilities. Non-procurement initiatives will aim at maximising the effectiveness of current and planned capabilities. ECAP Panels reports contain options to enhance and improve structures and to develop procedures and doctrine. 11. In this context, Ministers welcomed Member States commitment to the Headline Goal in the following ECAP Project Groups:

- Air-to-Air Refuelling (AAR); options for capability improvement could include multinational and national procurement, modification of equipment and via contracting and leasing;
- Combat Search and Rescue (CSAR); options for capability improvement could include development of equipment, doctrine and concepts, training and increased equipment interoperability;
- Headquarters (HQ); options for capability improvement could include implementation of national HQ plans, identification and training of augmentees and installation of communications infrastructure;
- Nuclear, Biological and Chemical (NBC) protection; options for capability improvement could include development of doctrine and concepts and through training;

⁸⁸ “Informal defence council devoted mainly to EU’s military capability”, *Agence Europe*, 14 March 2003

- Special Operations Forces (SOF);
- Theatre Ballistic Missile Defence (TBMD); options for capability improvement could include multinational and national procurement, training and further multinationalisation of headquarters;
- Unmanned Aerial Vehicles (UAV); options for capability improvement could include operational concept, certification in airworthiness and guidelines for procurement;
- Strategic Air Lift;
- Space based assets;
- Interoperability Issues and Working Procedures for Evacuation and Humanitarian Operations.

Ministers recalled that Member States participating to an ECAP Project Group should set and agree the objectives and milestones to be reached. In addition, Member States are invited to consider the lead or participation in further Project Groups such as in the areas of Attack Helicopters, Support Helicopters, Cruise Missiles and Precision Guided Munitions, Strategic Sea Lift, Intelligence Surveillance Target Acquisition and Reconnaissance (ISTAR).⁸⁹

The Declaration also formally declared that the EU had achieved an initial operational capability across the full range of Petersberg⁹⁰ tasks:

Based on the Forces contributed to the Helsinki Force Catalogue 2003, the current military assessment of EU military capabilities is that the EU now has operational capability across the full range of Petersberg tasks, limited and constrained by recognised shortfalls. These limitations and/or constraints are on deployment time and high risk may arise at the upper end of the spectrum of scale and intensity, in particular when conducting concurrent operations. These limitations and constraints on full achievement of the Headline and Capability Goals could be alleviated if the recommendations on meeting the shortfalls are followed- up. The impact of these limitations will need to be assessed case by case against the nature of each specific operation and its particular demands as well as envisaged contribution of required capabilities. Ministers therefore reaffirmed their strong commitment to reduce these limitations through all possible means.⁹¹

However, the announcement met with criticism from some Member States, the UK in particular. An article in *The Economist* noted:

On May 19th, Yiannos Papantoniou, defence minister of Greece (which holds the EU's rotating presidency), duly declared that Europe's army was now ready for action; and that this was "a great day, an historic day for the European Union".

⁸⁹ European Union, *Declaration on EU Military Capabilities*, 19 May 2003

⁹⁰ Petersberg tasks refer to the collective peacekeeping tasks allocated, originally to the WEU, in 1992. These operations consisted mainly of humanitarian intervention, crisis management and peacekeeping.

⁹¹ *ibid*

Not everyone was quite so sanguine. Geoff Hoon, Britain's defence minister, pooped the party, pointing out that it had taken Britain 70 days to deploy 45,000 troops to Iraq, and that there is a lot more to do if the EU's goal is to be met. Javier Solana, the Union's foreign-policy chief, said it needed to be done urgently.

The trouble is not the troops themselves: the force is not a standing army, waiting for its orders in barracks in Brussels, but an ad hoc coalition of suitable components. The trouble is the shortfalls in equipment which, despite years of ministerial talk about remedying them (and the possibility of borrowing some things from NATO), remain serious. The British are particularly worried about inadequate stocks of "smart" bombs, air-to-air refuelling capabilities, surveillance equipment and heavy-lift transport aircraft. The underlying problem is the reluctance of European governments to put their money where Mr Papantoniou's mouth is (in terms of both procurement and research) and duplication in what they do spend. Several governments this week blamed their predicament on the EU's Maastricht rules that govern public spending.

In practice, say the British, this means that the EU would struggle to perform the tasks at the tougher end of the Petersberg scale.⁹²

3. Six Nation Framework Agreement

In July 1998 the UK, France, Germany, Italy, Spain and Sweden signed a Letter of Intent (LOI) aimed at facilitating defence restructuring in Europe. That initiative was motivated by the need to retain competitiveness in Europe's defence industry following significant industry restructuring in the US and decreasing global defence budgets.

The LOI established six working groups to examine the main areas where the governments were committed to removing the barriers to restructuring. The results of these working groups were consolidated into a Framework Agreement which was signed in July 2000. The agreement created a framework for co-operation in the harmonisation of military requirements; security of supply; research and technology; export procedures; the security of classified information; and the treatment of technical information.

The Framework Agreement stated:

Security of Supply. Parties are committed not to hinder unnecessarily the supply of defence material to the other Parties; to consult on any merger or acquisition of defence companies that may threaten security of supply; and work together on providing supplies from national stocks; priority and allocation of supplies; and reconstitution of supply facilities.

⁹² "Ready or Not: European defence", *The Economist*, 24 May 2003

Exports Procedures. The Agreement commits participating nations to apply simplified export licensing arrangements to transfers made in the course of joint development and production programmes and to transfers for each others' national military requirements; and to develop lists of permitted export destinations for jointly produced military goods on a consensual, project-by-project basis. Export licensing decisions will continue to be taken according to the principles of the EU Code of Conduct on Arms Exports. The proposed arrangements will not abrogate existing national export controls.

Security of Classified Information; New simplified security provisions will be introduced for exchanges of classified information between countries or their defence industries that do not undermine the security of that information.

Treatment of Technical Information. The Agreement directs the Parties to harmonise their contracting processes for the disclosure, transfer, use and ownership of technical information to facilitate the restructuring and subsequent operation of the European defence industry.

Research and Technology. Co-ordination of joint research activities will be fostered to increase the advanced knowledge base and thus encourage technological development and innovation.

Harmonisation of Military Requirements. Parties are committed to further work on improving harmonisation of military requirements - an essential prerequisite to better equipment co-operation. It is envisaged this will lead to starting the process earlier through co-operative equipment planning to identify and formulate common military requirements with our partners rather than attempt to harmonise already mature "national" requirements.⁹³

Giving evidence to the Defence Select Committee inquiry on Defence Procurement, the Chief of Defence Procurement, Sir Peter Spencer, commented on the slow progress being made in the implementation of the Framework Agreement:

Starting with the European countries, the formal position today is that we have signatures from all nations except Italy have ratified the Framework Agreement and we expect them to complete the ratification process quite soon. The Agreement is broken into six areas of which five require further implementation arrangements and a couple of those are currently being circulated around the nations for signature and the others are well on the way. Frustratingly slow, if we wanted to have these arrangements in place immediately. I would put a more positive gloss on it, inasmuch as it is all very well having great headline arrangements, if they are not properly staffed or in detail, so the processes are understood by the people in the different countries, both in industry and in the government agencies as to how they are going to operate, we will not make any

⁹³ Ministry of Defence, *Explanatory Memorandum for an Agreement to Facilitate the Restructuring and Operation of the European Defence Industry.*

real progress. One of my priorities will be to continue to drive forward on that and to encourage my fellow National Armament Directors to push it forward as well.⁹⁴

In its conclusions the Defence Select Committee stated:

We welcome any initiative that encourages movement towards a rationalised and efficiently managed defence market in Europe. It is important, however, that any developments on that front do not create agencies and programmes which foster European preference at the expense of the UK's two-way trans-Atlantic trade.⁹⁵

Burkhard Theile concluded in an article in *Military Technology*:

The Agreement offers many possibilities for the effective and efficient operation of transnational defence companies in Europe and for better turnout of R&T budgets. A consolidated European defence industry has better economic chances than a fragmented industry. Commercially successful companies can afford to finance more R&T, this together with the harmonisation of European defence research are good conditions for a stronger European defence technology base [...]

The Framework Agreement should be regarded as a significant contribution to the European unification process, which adds a common foreign and security policy to the political and economic union.⁹⁶

4. UK/US Declaration of Principles

In February 2000 the US and UK signed a Declaration of Principles aimed at harmonising initiatives in areas comparable to those covered in the European Framework Agreement. (See Appendix One).

Following the signing of the Declaration those aspects dealing with export controls were taken forward under the Defence Trade Security Initiative (DTSI), which was approved by the UK and US in May 2000. Among other things, the DTSI examined the scope for introducing a waiver for the UK from US export control restrictions as set out in the International Trafficking in Arms Regulations (ITAR).

During 2000 the UK Government engaged in consultations with the US government on implementing DTSI. However, progress in implementing the UK/US Declaration of Principles and the DTSI, and on the ITAR waiver in particular, has been regarded by many analysts as slow and often non-existent.

⁹⁴ Defence Select Committee, *Defence Procurement*, HC 694, 23 July 2003

⁹⁵ *ibid*

⁹⁶ "Bridging the gap", *Military Technology*, 1 February 2002

In evidence to the Quadripartite Committee on 21 March 2002 the Director of International Security at the Foreign and Commonwealth Office, William Ehrman, stated:

The discussions (between the UK and) the United States on this issue are still continuing...the issues still to be discussed are some of the technical points relating to the compatibility of our export licensing regulations with the proposal of the US to allow unclassified equipment to come into this country.⁹⁷

In its most recent report of 20 May 2003 the Quadripartite Committee commented:

Negotiations with Australia on an ITAR waiver have now been completed. There have been unconfirmed reports in the specialist press that negotiations on a UK waiver will follow shortly, with an agreement in place by 2004. We hope that the reports are accurate that agreement is imminent on a British waiver from the International Trade in Arms Regulations. We recommend that the 2002 Annual Report should include a progress report on negotiations towards this waiver.⁹⁸

However, in May 2003 several newspapers reported that Congressman Henry Hyde, Chairman of the House International Relations Committee, had written to the US Secretary of State, Colin Powell, outlining the concerns of the committee over the granting of an ITAR waiver to the UK. An article in the *Financial Times* stated:

The US Congress is refusing to waive restrictions on the sale of military items to allow the administration to enter into defence trade agreements with its two closest allies in the war on Iraq, Britain and Australia.

The powerful House International Relations Committee this week rejected an administration request for such a waiver, saying that it could set a precedent for future agreements that might allow US weaponry to be diverted from Europe to US adversaries.

In a strongly worded letter to Colin Powell, the Secretary of State, Henry Hyde, the committee's chairman and a Republican, said that proposals to ease US export controls "seem unwise and particularly incongruous with the increased threats to US security and foreign policy interests since the attacks of September 11, 2001".⁹⁹

An article in *Defense News* also commented:

Hyde is concerned that allied efforts to align their defense trade policies with those of the United States fall short – particularly in Britain, where the primary

⁹⁷ Quadripartite Committee, *Annual Report on Strategic Exports for 2000 and Parliamentary Prior Scrutiny*, 21/3/02 Minutes of Evidence

⁹⁸ Quadripartite Committee, *Strategic Export Controls Annual Report for 2001, Licensing Policy and Parliamentary Scrutiny*, HC474, 20 May 2003

⁹⁹ "Congress snub for arms trade with allies", *The Financial Times*, 9 May 2003

legal recourse for US authorities in the event of an illegal transfer of US technology to a third party is governed by contractual agreements between the UK government and private British firms.

Further complicating the issue was the July 10 announcement of a federal investigation into 18 US companies that allegedly exported controlled sensitive technology to Iran through a UK front company. The announcement was a blow to the waiver effort, giving opponents of the agreement fresh ammunition to hinder the deal.¹⁰⁰

In a Written Answer on 2 June 2003 the Minister for the Armed Forces, Adam Ingram, stated:

United Kingdom and United States Government officials have recently agreed proposed texts for a waiver from the US International Traffic in Arms Regulations (ITAR). This will provide for export licensing requirements to be waived in respect of certain unclassified defence items and technical data exported to Her Majesty's Government and qualified companies in the UK, which would facilitate US/UK defence industrial collaboration. Work continues on regulatory and administrative implementation measures needed to complete the undertakings that have been agreed between the Governments. The US Government will respond to matters raised by the Congress about the terms of the agreement that has been reached.¹⁰¹

In its report on *Defence Procurement* in July 2003 the Defence Select Committee commented:

The US and UK authorities had largely secured agreement on the UK waiver in 2002, but then the Congressional approval process appears to have got caught in US domestic rivalries. Our Defence Industries Council witnesses highlighted that Congress had concerns about protecting US industry, and Lord Bach conceded that motives in the US on this issue were "mixed—some good, some not so good". Our industry witnesses also highlighted, however, that Congress had concerns about 'leakage' to some European countries—

One of the principal arguments that is deployed by the US in the context of maintaining its existing policies is the question of leakage...It is very much a hangover from the old Communist days when there were genuine and absolutely correct concerns about leakage into the Eastern Bloc countries. I have to say that I think in recent times, and certainly post September 11, these issues are more difficult to deal with than they were prior to that... There are some parts of Europe that are clearly more focused for attention than maybe they were a few months ago. These are all territories with whom we have important programmes in the UK [...]

¹⁰⁰ "US export relief for allies draws fire", *Defense News*, 21 July 2003

¹⁰¹ HC Deb 2 June 2003, c39W

Congress has to approve the text of the Waiver Agreement (now agreed between the US and UK sponsoring authorities) in both Houses, but in the House of Representatives the International Relations Committee has indicated its likely unwillingness to pass the Agreement. It has put a 'Chairman's marker' on the document which replaces the waiver with a counter-proposal to speed up the processing of licences for items to be exported to the UK to 10 days (from the current norm of perhaps five times as long). If the Senate and House persist in approving different forms of draft treaty, then a new compromise text will have to be prepared and returned for their consideration. In the meantime this year's House Armed Services Defense Authorities Bill includes provisions which could undermine the operation of an ITAR waiver, including a potential amendment to prevent the waiver superseding the test of US 'public interest' when applying the Buy American Act.¹⁰²

The committee concluded:

We are disappointed therefore about the suspicion with which some in Congress have viewed the ITAR waiver, not only because the benefits for both the US and UK remain unfulfilled, but more importantly because of the message that the delay conveys about the nature of the UK-US relationship.¹⁰³

Securing the ITAR waiver is considered by a number of analysts as essential for the British participation on programmes such as the Joint Strike Fighter. Many analysts have also suggested that the lack of progress on securing an ITAR Waiver for the UK does not bode well for progress on other aspects of the Declaration of Principles.

¹⁰² Defence Select Committee, *Defence Procurement*, HC 694, 23 July 2003

¹⁰³ *ibid*

III The 2002 Defence Industrial Policy

On 14 October 2002 the MoD published its Defence Industrial Policy, which seeks to link up current industry and government initiatives to provide a clearer framework for the defence procurement process, for defence research and development and to maximise the future competitiveness of the UK defence industry. The Defence Industrial Policy Paper can be accessed online from the Ministry of Defence website.¹⁰⁴

The main conclusions of the policy are as follows:

Acquisition

- There are four key factors which will be taken into account in acquisition decisions to ensure best value for money. These include:
 1. An assessment of the cost and operational effectiveness of project options. Estimates of whole life costs and the evaluation of risk are regarded as having increasing importance within this evaluation. This assessment would also include a judgement of the capability of a supplier to manage technological and commercial risk.
 2. The affordability of a solution.
 3. The wider long-term value for money of a solution. Any decision which would impact on future competitiveness, by creating a monopoly for example, would be taken into consideration.
 4. For national security reasons, high priority would be placed upon retaining a small number of strategic capabilities within the domestic industrial base. These would include capabilities in the fields of nuclear technology, defence against biological, chemical or radiological warfare and some counter-terrorist measures.
- The policy paper also sets out a number of wider defence and national interests that would be considered in any procurement decision. These include:
 1. Protecting security of supply in order to ensure that the MoD is able to support equipment in times of conflict. The MoD acknowledges that an increasing mutual reliance on security of supply is inevitable for all nations. As such, the best means of management of risk in this area is considered to be

¹⁰⁴ The MoD's Defence Industrial Policy Paper is available at:
http://www.mod.uk/issues/industrial_policy.htm

through collaborative agreements such as the European Letter of Intent Framework and the Declaration of Principles between the US and the UK.¹⁰⁵

2. Evaluating the level of investment the MoD has channelled into a project through its science and technology strategy.
 3. Assessing the future export potential of a solution. Exports can improve overall cost-effectiveness by reducing the unit cost and through the export levy on sales of equipment developed at Government expense. They can also improve the economic strength of the defence industry.
 4. Evaluating the extent (both quality and quantity) of industrial participation (IP) included in a solution.¹⁰⁶ The MoD regards IP as a means to encourage the transfer of technology and ensure investment in particular industrial capabilities in the UK.
 5. Evaluating whether it is desirable to retain a certain capability within the UK industrial base, outside of national security considerations. An industrial capability can bring for example, high-value to the industrial economy either because of its potential in world markets, its ability to transfer technology into wider commercial applications or its regional impact, including the number and quality of UK jobs that are created or sustained.
 6. Consideration for the UK's wider foreign and security policy interests. Many procurement programmes and collaborative ventures are large in scale and political importance, thereby having an impact on foreign policy.
 7. Taking into consideration the wider MoD policy framework. Certain procurement decisions may raise legal issues or affect/ be affected by the MoD's environmental, security, personnel or defence estates policies.¹⁰⁷
- More transparency and inclusiveness within the procurement decision making process will be introduced. The relevance of wider national interests to the outcome of a competition will be evaluated and explained to potential bidders at the earliest opportunity in the procurement process. This will allow potential bidders to frame their bids accordingly and so increase the efficiency of decision making. For example, the MoD has a stated policy whereby all Royal Navy

¹⁰⁵ See Section II C for more information on these initiatives.

¹⁰⁶ There are two types of industrial participation (offset): direct and indirect. The use of offset in defence procurement is now commonplace and most nations have some form of offset regulations with which potential foreign suppliers must comply. In some cases offset is required up to 100% of the contract value. More information on IP/ offset is available online at:

<http://www.tradepartners.gov.uk/countertrade>.

¹⁰⁷ Information on these policies is available online at: <http://www.mod.uk/issues/index.htm>

warships must be designed and constructed in the UK, therefore having implications for the procurement process.¹⁰⁸

- Open and fair competition, at both the prime and sub-contract level, will remain the bedrock of the MoD's procurement policies as a means to achieving the best value for money and developing an efficient and innovative industrial base.
- However, although competition remains important to the procurement process, the policy paper makes clear that the MoD will not use the competitive process where it offers no long-term advantage with regard to value for money or the retention of key UK defence industrial capabilities.
- The MoD remains committed to public/private partnerships and the Private Finance Initiative in the delivery of defence services.
- The MoD is also committed to earlier technology "de-risking" in procurement projects. Investment in this area is seen as a key tenet of Smart Acquisition and critical to ensuring the delivery of an effective military capability. For example, 15% of the budget for the Ground Based Air Defence (GBAD) programme is being invested in advance of the project's demonstration phase in order to reduce risk.

Research and Development

- Investment in research and technology is regarded as a critical factor in the future prosperity of the defence industry. However, the MoD has acknowledged that investment can not be made in every research sub-sector due to financial considerations. Therefore, the prioritisation of resources into specialised areas will form the backbone of the MoD's future Research and Technology Strategy. These areas include capabilities deemed to be of critical military importance or commercially advantageous. Partnering with industry is also seen as a key element of this strategy.
- The MoD has established two principal schemes to support the policy of partnership with industry and to facilitate the development of particular technologies.
 1. The Towers of Excellence (TOE) programme, which was established following the 1998 Strategic Defence Review (SDR), seeks to focus technological priorities in a number of areas. Six have already been identified:

¹⁰⁸ HC Deb 15 July 2002, c19W

guided weapons, radar, sensors, electro-optic capabilities, underwater sensors and synthetic environments.

2. The Defence Technology Centres (DTC) project has established a number of collaborative arrangements between industry and academics, jointly funded by the participants and the MoD, with the aim of generating and exploiting future technologies.¹⁰⁹
- The policy paper advocates maximising the exploitation of civil technology, especially in the high-value communications and aerospace sectors. Taking advantage of evolving civil technology is regarded as essential for freeing public resources for the development of defence-specific technologies where the private sector is unable or unwilling to invest.
 - International collaboration in research and development is regarded as an important means of filling gaps in the UK's domestic technology base. One element of the European Letter of Intent Framework is to identify areas in which government-industry research collaboration can take place on an international level, and develop the means for partner nations to access a common pool of technology.
 - With the collective defence research budget of Europe equating to approximately one third of the US defence research budget, the MoD recognises the need to maintain access to US technology. The policy paper highlights that an agreement has been reached, in principle, between the UK and the US on increasing the proportion of transatlantic research collaboration.

Future Competitiveness

- The main role for the MoD in ensuring future competitiveness of the industry, and maintaining access to first-class technological capability, is to ensure access to wider markets. The political dimension of this role is through the creation of appropriate regulatory environments, the harmonisation of military requirements, potentially leading to collaborative projects and the abolition of protectionism in foreign markets.
- With regard to the United States, the MoD will continue to press for the freer flow of technology created on both sides of the Atlantic. The UK has already signed a Declaration of Principles with the US which commits both governments to improving transatlantic defence. A key aim is to conclude ongoing negotiations on

¹⁰⁹ More information on the Towers of Excellence programme and the Defence Technology Centres can be located on the MoD website at: <http://www.mod.uk/toe/index.html> and <http://www.mod.uk/dtc/index.html>.

the International Trafficking in Arms Regulations (ITAR) exemptions, which would allow the export of unclassified defence items and technology to UK companies without the requirement for a US export licence.

- The MoD is committed to improving the performance of the European defence market, while also harmonising European military requirements in order to benefit from economies of scale in a period of financial constraint. The six-nation Letter of Intent Framework seeks to address the issues of security of supply, the regulation of export procedures, streamlining research and development budgets and the harmonisation of military requirements. The MoD will also continue to promote in Europe the liberalisation of rules governing the ownership of defence companies and encourage European allies to reduce their state shareholdings in these companies. The UK Government is also supportive of the development of the multilateral procurement management body, OCCAR, in order to reduce delay in collaborative programmes.

Work is also underway through the NATO Prague Capabilities Commitment (PCC) and the EU Capabilities Action Plan (ECAP), to harmonise military requirements. See section II C.

- In order to maintain dialogue between the Government, industry and other stakeholders in the area of defence exports, the Defence Export and Market Access Forum will be established.

Announcing the defence industrial policy on 14 October 2002, the Secretary of State for Defence, Geoff Hoon, commented:

The Government is committed to a strong and globally competitive UK defence industry. We all benefit from its high-value, technology skill base. Our new policy demonstrates our drive to provide high quality equipment for the Armed Forces whilst promoting the interests of British industry and maximising the economic benefit to the UK from our defence expenditure. It has been drawn up in consultation with industry, and will maintain this close dialogue as we take this policy forward.¹¹⁰

The policy has been generally welcomed by analysts and the defence industry.

An article in *The Guardian* on 15 October 2002 suggested:

The government yesterday threw a lifeline to the embattled defence industry by tempering its obsession with competition at all costs and emphasising the need to

¹¹⁰ Ministry of Defence Press Release, 14 October 2002. Available online at: <http://213.38.88.204/802566FC004AC1A9/Search/C2B1EA4A4D0C422C80256C5200440256?OpenDocument>

sustain Britain's industrial base. Geoff Hoon, the Defence Secretary, set out the first defence industrial policy in years after being pressed by disgruntled companies during the past 18 months to do so.¹¹¹

On 23 October 2002, *Jane's Defence Weekly* commented:

In a change widely welcomed by defence industry executives, the UK Ministry of Defence has announced new procurement guidelines that clarify existing policies and make explicit the weight of preserving the UK defence industrial base in competitions...the clearer policy was seen by defence industry experts as a boost to Thales– the second largest MoD contractor– and the UK units of US companies. It was also viewed as a mild slap to BAE SYSTEMS, which has argued that the MoD should rely more on non-competitive awards both to ease the cost of the bidding process and preserve the UK's defence industrial base...The question, however, remains over how the policy will be put into effect. A senior Lockheed Martin official said that the message of the new policy, at first sight, seems a good turn for the industry but the true impact will be seen in the details of its implementation.¹¹²

In its July 2003 report on *Defence Procurement* the Defence Select Committee concluded:

We very much welcome the publication of the Defence Industrial Policy, bringing as it does a useful, though long overdue, increase in transparency to this important area. The way its provisions and statements should be interpreted will inevitably have to be developed; by further debate and through "case law". Indeed, in some areas, including the use of competition and open markets and in risk management (two of the perhaps more contentious of its themes) [...] the Policy's utility will be evident only with the passage of time. It does however provide a helpful launch-point for developing policy in this important area.¹¹³

The success of the Defence Industrial Policy has recently been assessed by many analysts against the MOD's decision in July 2003 to award a contract to BAE Systems for an advanced jet trainer for the RAF and Royal Navy. Subject to successful contract negotiations the MOD intends to initially purchase 20 aircraft, with the option of procuring a further 24 at a later date. The deal is worth £800 million (£3.5 billion through life) and the Hawk 128 is expected to enter service in 2008.

¹¹¹ "Hoon Puts Defence Jobs Ahead of Competition", *The Guardian*, 15 October 2002, p.20

¹¹² "UK Spells Out New Defence Procurement Policy", *Jane's Defence Weekly*, 23 October 2002, p.19

¹¹³ Defence Select Committee, *Defence Procurement*, HC694, 23 July 2003

Announcing the decision the Secretary of State for Trade and Industry, Patricia Hewitt, stated:

This was a very tough decision but underlines our commitment as a Government to the new defence industrial policy and manufacturing strategy. Hawk bring major economic benefits to Humberside and wider to the UK through key suppliers. Hawk is a good aircraft with significant export potential for the UK.¹¹⁴

However, while some analysts have argued that the decision is supportive of the approach laid down in the MOD's defence industrial policy, others have suggested that the Hawk deal is protectionist and contradictory to the ideas of achieving best value for money.

An article in the *Financial Times* prior to the announcement suggested:

The intensity of the political battle over Hawk jets, which has pitched Gordon Brown against four cabinet colleagues, reflects the wider implications of the deal. Tony Blair's decision on whether to hand the multi-billion pound contract to BAE Systems will set an important precedent for defence spending. The prime minister is faced with an essentially simple choice when he deals with the Hawk papers waiting on his desk. Should the government opt for the cheapest deal that offers the technical capabilities it needs? Or should it pay more to safeguard thousands of jobs, skills and potential future export orders?

The deal has acquired huge political resonance principally because it puts two key factors - the Treasury's pet criterion of value for money versus British jobs and orders - into clear conflict. A defence insider said: "I can't think of any recent procurement where we've been faced with such a stark choice. Usually there's an obvious winner." [...]

The defence industrial strategy launched by the government last year was meant to resolve such dilemmas. Hailed by defence companies and unions - and trade ministers - as a victory for UK manufacturing, it promised procurement decisions would take into account industrial capabilities and export potential as well as value for money. The problem is the policy failed to spell out which factor should take priority.

Flight International commented:

Although the Ministry of Defence is keen to stress that the Hawk 128 is the best aircraft for the job, this deal is widely seen as a significant shift in policy - ensuring that UK industry is supported by Whitehall spending. This will be condemned in many quarters but it is nothing that the majority of governments do not do already. The policy is also one repeatedly called for by UK companies and industry bodies in recent years [...]

¹¹⁴ Ministry of Defence press release 172/03, 30 July 2003

Competition will still be the usual means of selecting defence contractors, but the impact of the [Hawk] competition on UK industry should receive greater attention. And despite the intent to protect UK jobs, it should be remembered that competition is a good thing. In the early stages of competition it fuels innovation. Later it helps control costs and drives bidders towards meeting desired in-service dates [...]

If industrial issues are to be more centre stage during procurement, then it is likely that national champions will emerge.¹¹⁵

An editorial piece in the *Financial Times* also argued:

What should have been a routine decision to buy 20 training jet aircraft needed by the armed forces has turned into a surprise test of the government's ability to spend money efficiently and resist propping up failing industries. Unfortunately, yesterday's promise to spend up to £800m on 44 Hawk jets to preserve jobs at BAE Systems shows that Ministers have failed a crucial challenge [...]

Geoff Hoon's battle to keep the union's happy at a crucial time in his own career means that his department will now have to fund the extra cost out of its existing procurement budget. The MOD is also left vulnerable to BAE bullying in the future [...] Now, at just the time when it [BAE] should be punished for cost overruns and delays incurred on such uneconomic programmes, the government's weakness has cost us all dear.¹¹⁶

¹¹⁵ "National champions", *Flight International*, 5 August 2003, p.3

¹¹⁶ "Hawk climbdown", *The Financial Times*, 31 July 2003, p.16

Appendix One – UK/US Declaration of Principles, February 2000

The Department of Defense of the United States of America and The Ministry of Defence of the United Kingdom of Great Britain and Northern Ireland (5 February 2000)

DECLARATION OF PRINCIPLES FOR DEFENSE EQUIPMENT AND INDUSTRIAL COOPERATION

The Governments of the United States of America and the United Kingdom of Great Britain and Northern Ireland have a longstanding cooperative relationship across a broad spectrum of defence activities, including strict enforcement of export policies for armaments and technologies; strong industrial security systems and compatible industrial security practices; close relationships in law enforcement and cooperation on industrial security matters and export control violations; and close relationships in intelligence sharing on matters of counterintelligence and industrial security, and countering economic espionage and export control violations. Moreover, the Department of Defense of the United States of America (U.S. DoD) and the Ministry of Defence of the United Kingdom of Great Britain and Northern Ireland (U.K. MoD) desire to maximize value for money in defense equipment acquisition, based on the principle of competition.

Our relationship is underpinned by the Memorandum of Understanding between the Department of Defense of the United States of America and the Secretary of State for Defence of the United Kingdom of Great Britain and Northern Ireland concerning Principles for Research, Development, Production and Procurement, dated December 13, 1994, and other bilateral arrangements and agreements.

Our past efforts to improve the level of defense equipment cooperation and trade have not realized their full potential. Nonetheless, we believe that it is fundamental to our common interests to enhance the environment for mutual defence equipment and industrial cooperation. We therefore intend to improve significantly the cooperative framework that will facilitate both traditional and new types of collaboration by our defense companies and a more integrated and stronger industrial base. It is also our intention to take the necessary steps to ensure that U.K. industry doing business in the United States will be treated no less favourably than U.S. industry doing business in the United Kingdom. We believe that this initiative will provide an important and welcome opportunity to enhance our mutual interdependence in the defense equipment field.

The U.S. DoD and U.K. MoD intend to apply the provisions of this Declaration and Annex to those matters within their respective areas of responsibility. They affirm the prerogatives of other agencies of their respective governments on certain matters related to this Declaration and Annex and note that in the case of the United States, the provisions of the Declaration and Annex do not apply to matters that are under the jurisdiction of other agencies of the government including the Department of State. They also note that within their respective governments there is ongoing work related to such

matters to further the objective of cooperation between their governments, the outcome of which is not prejudiced by the provisions of this Declaration and Annex. They also affirm their desire to promote similar cooperation between each of them and other allies, both bilaterally and multilaterally.

Therefore, the U.S. DoD and U.K. MoD have reached the understandings reflected in this Declaration of Principles and its Annex attached hereto. The principles established in this Declaration and in the Annex to this Declaration, which is an integral part of the Declaration, are not intended to be legally binding, nor to entail new fiscal obligations on the part of either the U.S. DoD or the U.K. MoD, but to point the way to arriving at future arrangements or agreements which may be legally binding. It is further understood that these future arrangements or agreements may entail amendments to national laws or regulations.

Signed in duplicate at Munich, Federal Republic of Germany, on the fifth day of February 2000.

Geoffrey Hoon

Secretary of State for Defence United Kingdom of Great Britain and Northern Ireland

Williams S. Cohen

Secretary of Defense United States of America

Annex

PURPOSE

1. The purpose of this Annex to the Declaration of Principles (Declaration) is to indicate the areas in which the US DoD and the UK MoD ("the Participants") intend to find common solutions to the problems identified; to define the principles on which appropriate follow-on arrangements or agreements, or amendments to existing arrangements or agreements, will be based; and to establish a process and intended timescale for the negotiation of follow-on arrangements or agreements, or amendments to existing arrangements or agreements, to implement these principles.
2. This Declaration is intended to establish principles for future arrangements or agreements, or amendments to existing arrangements or agreements, which may cover the industrial, investment, and export sectors of defence in both countries.
3. The Participants have the firm intention to pursue the objectives of this Declaration and to adopt, where appropriate, specific arrangements or agreements, or amendments to existing arrangements or agreements between them, to underpin the effective application of the principles specified in this Declaration.

HARMONISATION OF MILITARY REQUIREMENTS AND ACQUISITION PROCESSES

1. The Participants will seek better means to harmonise the military requirements of their armed forces. To this end, and proceeding from identified capabilities of common interest, the Participants will identify areas in which better harmonisation is considered possible. In doing so, they will seek to make use of existing fora, wherever practicable.
2. The Participants will identify projects at an early stage for cooperative research, development, production, and procurement. (See Research and Development, below.)
3. The Participants will examine the possibility of harmonising the procedures applicable to armaments acquisition, so as to remove impediments to effective cooperation.

MEETING NATIONAL DEFENCE REQUIREMENTS

1. Each Participant will require assurance that the other Participant will facilitate the supply of certain specified defence articles and defence services necessary to discharge their national security and foreign policy commitments. The Participants acknowledge that this assurance of supply is as important for industry as it is for governments, if industry is to adapt to the process of globalisation.
2. The Participants recognise the potential for a degree of interdependence of supplies needed for national security. In order to achieve acceptance of this concept, the Participants will explore solutions for achieving assurance of supply for both Participants. These solutions may include obtaining assurances, some of which may be legally binding, relating to the supply of defence articles and defence services, including technical data, agreed upon by the Participants.
3. To further enhance this assurance, and with due consideration for the right of each Participant's government to control the disclosure and use of technical information, arrangements will be considered to enable the other Participant to reconstitute, in exceptional circumstances to be defined, an indigenous supply of a particular defence article or defence service.

EXPORT PROCEDURES

1. The Participants confirm their desire to maintain a strong defence industrial capability as part of their industrial bases and the ability to export defence articles and defence services. Consistent with the intent of this Declaration, they will explore possible approaches to achieving greater transparency and efficiency in their national procedures for exports of defence articles and defence services.
2. The Participants will explore means of simplifying the procedures for export of defence articles and defence services between themselves for their own use.

3. The Participants desire to see an improvement in the efficiency of the procedures for exports of jointly produced military goods to third parties. They will therefore examine the scope for establishing a procedure based on mutually agreed lists of acceptable export destinations for jointly developed and produced military goods and technologies on a project by project basis. These lists would be updated on a continuing basis.
4. The Participants will seek to ensure that their national laws and regulations for defence exports to third parties are implemented in a spirit of cooperation and with maximum efficiency. They will reinforce their cooperation and promote convergence in the field of conventional arms exports. They will pursue necessary measures to harmonise their conventional arms export policies as far as possible and examine means of establishing common standards of implementation.
5. The Participants will establish a high-level council on export control and coordination measures, with a view towards accomplishing the preceding measures.
6. Pending agreements reached pursuant to paragraph 5, above, re-transfers by a Participant of defence articles and services, including technical information, originating in the territory of the other Participant will be made in accordance with existing agreements, arrangements, contracts and procedures between the Participants.

SECURITY

1. The Participants recognise the need to ensure that adequate and appropriate security provisions for the protection of classified information are in force in any relevant US or UK company, regardless of any multinational aspects of a company's ownership or management structure. The Participants will endeavour to avoid placing unnecessary restrictions on the movement of staff, information, or material between the Participants or their industry.
2. The Participants will examine means to expedite the transmission of classified information between themselves or between their industries while maintaining the requisite degree of security protection.
3. In doing so, consistent with the General Security Agreement of 1961 between the Governments of the United States of America and the United Kingdom of Great Britain and Northern Ireland, the Participants will ensure that no classified information is passed to companies or persons not suitably cleared or needing to receive it; that no classified information originated by one Participant is passed to a third country national without the consent of the originating Participant; and no information carrying national caveats is passed to foreign nationals.
4. Consistent with the preceding paragraphs, the Participants will use their best efforts, both individually and working together, to lessen the administrative burdens placed on their industry in the establishment and oversight of industrial security measures.

5. The Participants intend to develop procedures to streamline the process for approving visits to government or contractor facilities by employees of the government or contractors of the other Participant that may involve access to classified information.
6. The Participants will jointly address security vulnerabilities posed by new technologies.
7. The Participants will endeavour to harmonise and streamline their security regulations.

OWNERSHIP AND CORPORATE GOVERNANCE

1. The Participants believe that the ownership of defence companies sited in the United States and the United Kingdom is a matter for the companies to determine, subject to the application of the relevant national merger control, anti-trust and other relevant laws. They wish to encourage the freest possible cross-border investment in defence-related industry.
2. While considering the implications for national security of any proposed international merger or acquisition, the Participants will not place unreasonable or unnecessary security restrictions on corporate governance.
3. The Participants will seek to establish arrangements or agreements whereby, on a reciprocal basis, each Participant will apply substantially the same standards in the granting of facility security clearances to companies that are organised and incorporated within its territory but are owned or controlled by entities within the territory of the other Participant, considering, among other factors, any connection with entities owned, controlled, or influenced by entities of any third country. These arrangements or agreements will include measures to address issues of corporate governance as well as security of information held by companies and compliance with national export control regimes.

RESEARCH AND DEVELOPMENT

1. The Participants recognise that technology, research and development are indispensable for maintaining an effective defence industrial base and therefore recognise the need to use the limited resources available for defence-related research and development in an efficient and effective manner.
2. In the context of this Declaration, the Participants intend to establish arrangements or agreements and make use of existing fora to:
 - (a) harmonise research and development programmes and exchange information about national research activities where there are common interests with a view towards setting common objectives for research and development, avoiding unnecessary duplication of effort or major gaps in technology and technical capability, and making the most effective use of dual-use and commercial off-the-shelf (COTS) technology;

- (b) increase cooperation in programmes that follow-on from research activity, in particular by undertaking technological developments with each other; and
- (c) ensure the adequate funding, and efficient cost sharing, of cooperative research and development.

TECHNICAL INFORMATION

1. The Participants confirm their desire to maximise the flow of technologies and technical information between themselves and between their defence-related industries. Accordingly, they will explore methods that could facilitate the flow of technologies and technical information between them and between their defence-related industries, while ensuring that the further flow of these technologies and technical information is strictly regulated by the governments. (See Export Procedures, above.)
2. These methods could include, where appropriate, the removal of unnecessary controls on the flow of technology and technical information, different ways to authorise the flow of technology, and different ways to optimise the exploitation for defence of technology investments.
3. The Participants will seek the establishment of arrangements relating to the disclosure, transfer, and use of technical information which will facilitate the efficient operation of US and UK defence companies, consistent with proper safeguards. The Participants recognise that technical information received from the other Participant shall not be further disclosed without the authority of the owner and, in the case of classified or export controlled unclassified information, without the authority of that Participant under whose authority the information was created.
4. The Participants will encourage the harmonisation of their laws, regulations, and procedures for controlling disclosure and use of technical information in the field of defence.

PROMOTING DEFENCE TRADE

1. The Participants will, on a reciprocal basis, endeavour to diminish legislative and regulatory impediments to optimising market competition.
2. The Participants will endeavour to revise their acquisition practices to remove impediments to efficient global market operations and to support reciprocity of international market access for each other's companies.
3. The Participants will give full consideration to all qualified sources in each other's country in accordance with the policies and criteria of the purchasing government.
4. Each Participant will explore means to eliminate laws, regulations, practices and policies that require or favour national industrial participation in its defence acquisitions.

TIMETABLE

1. Policy-level discussions concerning the principles underlying this Declaration and its Annex and the intended US-UK cooperation and collaboration in facilitating the restructuring of their defence industry will be carried out by appropriate national authorities.
2. Working-level discussions will be held by working groups of subject matter experts, which may include representatives from other government agencies. These working groups may consult with the Participants' defence industries, as appropriate.
3. It is the intent of the Participants that the agreements and arrangements, or amendments to existing agreements or arrangements, envisioned by this Declaration and its Annex be put in place as expeditiously as possible. Accordingly, they will endeavour to develop such agreements and arrangements so that they can be presented to the Secretary of Defence and the Secretary of State for Defence within one year after signature of this Declaration and its Annex. In addition, they will make periodic reports to the Secretary of Defence and the Secretary of State for Defence on the progress that is being made on achieving the goals of this Declaration and its Annex.

Appendix Two – Glossary of Terms

CCC – EU Capabilities Commitment Conference
CIC – EU Capabilities Improvement Conference
DCI – Defence Capabilities Initiative
DEC – Director Equipment Capability
DLO – Defence Logistics Organisation
DOP – Defence and Overseas Planning Committee
DPA – Defence Procurement Agency
DTSI – Defence Trade and Security Initiative
EAC – Equipment Approvals Committee
ECC – Equipment Capability Customer
ECAP – European Capabilities Action Plan
EOI – Expressions of Interest
ETAP – European Technology Acquisition Programme
IAB – Investment Approvals Board
IPT – Integrated Project Team
IPTL – Integrated Project Team Leader
ITAR – International Trafficking in Arms Regulations
ITT – Invitations to Tender
LOI – Letter of Intent
NATO – North Atlantic Treaty Alliance
OCCAR- Organisation Conjointe de Coopération en Matière d’Armement
PCC – Prague Capabilities Commitment
PE – Procurement Executive
PFI – Private Finance Initiative
QMV – Qualified Majority Voting
SDR – Strategic Defence Review
SPI – Smart Procurement Initiative
SRD – Systems Requirement Document
URD – User Requirements Document