CARNEGIE EUROPE

OCTOBER 2019

The European Commission in EU Defense Industrial Policy

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The European Commission will soon have a new Directorate General for Defense Industry and Space, as announced by President-elect Ursula von der Leyen on September 10. The idea is not new, but it received new momentum with the launch of the European Defense Fund (EDF) in 2017, which marked an unprecedented shift toward "more EU" at the level of defense industrial policy. This article looks at how the European Commission's role in EU defense policy has evolved, specifically with regard to market regulation, capability development, and arms export policy. The commission has gradually extended its reach but remains restricted in its influence, and it will have to prove its added value not just to Europe's defense firms but also to the EU's pursuit of becoming a more capable defense actor.

MARKET INTEGRATION

Seeing that defense had been largely excluded from the EU's market integration dynamics, the European Commission in the early 2000s set out to counter the problems of fragmentation, duplication, and protectionism that beset the European defense market. The commission's solution was to seek to create an integrated market with free movement of goods and services as well as open public procurement. Its most important move was to pass regulation dealing with the sector through the 2009 defense package, including two directives on the procurement and transfer of defense-related products. The goal was to increase competition and create economies of scale that would eventually lead to lower defense costs for EU member states.

The directives have had limited success. Member states continue to sidestep the internal market provisions of the EU treaties by invoking Article 346 of the Treaty on the Functioning of the EU, which allows any government "to take such measures as it considers necessary for the protection of the essential interests of its security." Governments have mostly applied the procurement directive's provisions to contracts that deal with maintenance and repair, facilities management, or the acquisition of equipment with low strategic value—

most major military-equipment contracts, even after the defense package, continue to be awarded without an EU-wide tender.

In 2018, the commission for the first time opened infringement procedures against five member states for breaches of the procurement directive. If these countries repeatedly fail to comply, it may refer the matter to the European Court of Justice. Because of the sensitive and highly political nature of procurement decisions however, there has been little willingness on the commission's part and that of defense companies to contest decisions by member states and take them to the court.

RESEARCH AND DEVELOPMENT

Most recently, the European Commission has targeted low and inefficient defense spending, particularly on research and development. As a European Court of Auditors report recently put it, to meet NATO's benchmark of spending 2 percent GDP on defense, EU members of NATO would have to invest an additional €90 billion (about $100 billion) annually, which would be a 45 percent increase compared to their 2017 spending. Many of them also subsidize uncompetitive defense industries as job creation schemes or buy equipment off-the-shelf from third countries, mainly the United States, instead of cooperating with their European allies. And according to data from the European Defense Agency (EDA), research and technology as a percentage of total defense spending has been steadily decreasing since 2006. Based on EDA estimates, the share of total defense spending dedicated to research and technology in 2016 was the lowest since 2006, at 0.77 percent. In 2017, it is estimated to have slightly increased to 0.80 percent.

The European Commission laid the groundwork for its involvement in security and defense spending in the late 1990s and early 2000s. It launched a Preparatory Action in Security Research in 2003 and the EU-wide Policy and Research in Security Program in 2007. The inclusion of dual-use technology in the latter allowed the commission for the first time to reach into the security and defense spending realm.

In 2015, the European Commission set up a high level "group of personalities," consisting of politicians, academics, think tank experts, and CEOs from research technology organizations and the defense industry, to advise on how the EU can support defense research programs relevant to its Common Security and Defense Policy. European Commission President Jean-Claude Juncker appointed a special adviser on defense and security policy for the first time. In 2016, the commission launched the European Defense Action Plan to support the competitiveness and innovation of the defense industry and the development of a strong defense technological and industrial base. Finally, in 2017, the commission launched a proposal for the EDF to be included in the EU's next multiannual financial framework, for 2021–2027.

The EDF represents a qualitative shift in the way the EU gets involved in defense. Through it, the European Commission wants to incentivize member states to spend more on defense-capability research and development, and to spend more wisely by working together. The EU plans to spend €8.9 billion (about $9.8 billion) to co-finance collaborative capability-development projects and €4.1 billion to fund collaborative defense research between 2021 and 2027.[1] A sum of €13 billion over seven years is not massive considering that the total combined defense spending of the EU member states is around €200 billion—but it is a start. The EDF would place the EU among the top defense research and technology investors in Europe and ideally encourage more spending by member states, especially if they use it to get co-financing for some of the projects planned in the Permanent Structured Cooperation format, under which they can work in smaller groups on more ambitious capability projects.

In brief, through market regulation and monetary incentives the European Commission has progressively been carving out a role for the EU in order to try to address some of the underlying problems that weaken the European defense technological and industrial base. But its power has limits.

ARMS-EXPORT POLICY

In order to convince member states to agree to the European Defense Fund, the EDF regulation states that receiving EU funding should not affect decisions regarding arms exports. This is the result of rigorous opposition from member states, in particular France, to any EU authority over exports. In fact, arms exports have repeatedly been excluded from EU treaty provisions, as governments are unwilling to give up their autonomy in this sphere.

Member states have agreed to uphold "high common standards" for transfers of conventional arms. This commitment is established at the international and EU level through the Arms Trade Treaty and the EU Common Position on Arms Export Controls. The latter sets out eight criteria against which member states must test export licenses, including respect for human rights and international humanitarian law in the destination country. But, although the common position is legally binding, member states are free to decide how they implement it, and there is no EU mechanism to sanction noncompliance. As a result, European arms-export policies are divergent, driven by commercial and national interests.[2]

This undermines Europe's common foreign and security policy goals. Export bans on arm sales by individual countries are less effective than those done in unity. If the European Commission wants to make defense industrial integration work, there is no way around member states embracing a more joined-up arms-export policy. Exporting to third countries allows defense companies to enlarge their customer base and creates economies of scale. It also incentivizes European firms to make more competitive products. The success of an instrument such as the EDF depends on a previously agreed, reliable, and consistent export policy at the EU level, otherwise future joint armament projects run the risk of falling flat. This is because member states will only join forces to develop new military equipment or weapon systems if they trust each other to provide the necessary components in times of crisis—to each other and to customers outside the EU.

The European Commission has been carving out a role for itself in dual-use export control. Controlling the trade in dual-use items is an EU competence; these items are regulated as part of the union's common commercial policy. Council Regulation 428/2009 (Dual-Use Regulation) lists controlled items. The commission has tightened the regulation of cyber-surveillance equipment, which could bolster its ability to add items to the dual-use list.

To ensure that member states adhere to the Common Position on Arms Exports, the EU would have to introduce a mechanism to hold governments accountable for breaking the rules. This could be a supervisory body, controlled by itself or the high representative for foreign affairs and security policy, to report violations and to refer member states to the European Court of Justice. However, these measures would require a change to the fundamental EU treaties and therefore unanimity among member states, and there is no political will in member states to give up power to the commission in this field.

WHAT RATIONALE, WHAT ROLE?

The European Commission had worked to gain more authority over defense industrial policy for decades, with limited success. The EU "defense momentum" that took place over the last three years was partly driven by crises in its eastern and southern neighborhoods, terrorist attacks in Europe, and—perhaps most importantly—the perceived weakening of the U.S. security guarantee. Through the launch of the Permanent Structured Cooperation format, the French-led European Intervention Initiative, the NATO-led Military Mobility program, and the EDF, governments reacted to the changing threat environment. At the same time, the United Kingdom's 2016 referendum on leaving the EU brought new attention to finding a European project to further integration, and some governments saw security and defense policy as having the most potential. In this context, the integration of defense policy was seen as a measure to promote cohesion among member states. There was also a clear economic motivation behind the drive for EU-level defense spending, with the European defense industry challenged by international competition and ever-dwindling domestic investment in research and development. Governments with the political will to integrate were then able to access the plans put together by the commission in preparation.

The European Commission does not have a mandate for military and defense policy. The legal basis for its activities related to the EDF is not the treaty elements associated with foreign and security policy, but rather Articles 173 and 182 of the Treaty on the Functioning of the EU, which relate to economic activities, specifically on enhancing industrial innovation and competition. As a result, the commission has an imperative to approach defense industrial policy through an economic policy lens, with the objective of strengthening Europe's defense technological and industrial base. The economic dimension is not only the legal basis for the commission's involvement but also where it has the most expertise.

At the same time, the EDF is explicitly geopolitical. Though its origins precede the EU's Global Strategy that was agreed in 2016, the fund was presented as one of the tools to implement it. The strategy outlined the ambition of strategic autonomy for the union—a contentious concept that has many different definitions but can be understood as the ability for the EU to act with partners if possible but alone if necessary. The EDF is meant to provide the industrial dimension of strategic autonomy, which for some governments and commission officials entails establishing a defense industry that can single-handedly produce the equipment and the capabilities that European countries require to defend their territory and their interests. In order to be successful, the EDF's priorities should relate directly back to the level of ambition outlined in the Global Strategy—as well as address NATO's critical capability gaps.

An early test case of how to navigate the divide between the strategic and economic rationales of the European Commission's involvement is playing out in the negotiations between the EU and third countries that have an interest in the European defense market. The participation criteria for the EDF specify that only collaborative projects involving firms from member states or associated countries—Norway, Iceland, and Liechtenstein—shall receive the EU's support. Cooperation between EU defense companies and third-country firms is not excluded, as long as the latter's involvement does not put the union's security interests at risk. But in practice this means that non-EU firms—for example, those based in the United States or the United Kingdom after Brexit—would not receive any EU funding. While they could technically participate in cooperative projects, they would have limited incentive to do so, with no access to sensitive information or control over intellectual property.

As a result, the United States has cautioned EU member states to open up their defense industrial ambitions to non-EU players. Americans have criticized the EDF's strict rules on intellectual property right and stressed that European countries limited to just their own market would miss out on technological evolution and lose U.S. interoperability. The United States is concerned that the EU's ambitions for industrial autonomy could lead to shutting out third countries that want to contribute, even at the risk of missing out on the latter's industrial expertise. The United States maintains that it supports the EU's efforts to "do more" on defense—as long as those neither duplicate nor undermine those of NATO—but it argues that the union's posture could be strengthened by ensuring that European governments keep buying U.S. kit off-the-shelf. A 2018 report by the American Chamber of Commerce to the European Union warns that if European policymakers were to pursue a Buy European Act in the defense sector, the United States could retaliate by closing off its own market to European companies.

The United Kingdom has found itself in a similar situation. After the Brexit referendum, it expected defense policy to be a comparatively straightforward part of the negotiations over its leaving the EU. However, it has since undergone the difficult experience of negotiating access to an EU defense industrial policy that is in the process of becoming less flexible and intergovernmental and more institutionalized, with a bigger role for the European Commission. The row between Brussels and London over UK participation in the EU's Galileo program was an early example of the difficulties both sides ran into in attempting to navigate this new terrain. The United Kingdom is also worried about the possibility that after leaving the EU it might be excluded from new multilateral capability-development projects funded with help from the EDF and with commission involvement. These could potentially include the fighter jet being developed by France, Germany.

Some member states have raised objections to the EU's strict approach vis-à-vis third states. Countries such as the Czech Republic, the Netherlands, Poland, Romania, and Sweden, whose defense industries need to maintain close links to U.S. and UK defense companies, have been able to influence the European Commission, which rejected the idea of a Buy European Act, with one official asserting that "the EU as a whole cannot afford to restrict public procurement." Von der Leyen, while clearly committed to the EU's defense efforts, has said that "the European Union will never be a military alliance," and that "NATO will always be our collective defense."

The commission is careful to stress that it is not excluding anybody from the EU's defense market, but rather pursuing reciprocity—setting conditions for companies to receive EU funding that are similar to the ones that European companies face in third countries such as the United States. The U.S. market is particularly closed off to outside firms—but the more important point is that European defense firms are currently unable to produce much without relying on U.S. components. The outcome of the negotiations between the EU and third countries as well as the degree to which member states will stick to the European Commission's guidelines for cooperation with third countries will serve as indicators of its influence going forward.

WHAT DOES SUCCESS LOOK LIKE?

The European Defense Fund is a test case for the European Commission's involvement in defense industrial policy. One important function of the EDF is to boost the EU's defense industrial base, but in many cases European countries will not be able to afford spending all their financial and political capital on EU-only projects that will take years—and sometimes decades—to be developed, at the expense of much-needed capabilities that can only be provided by third country industries.

What matters in the long term is the capacity to invest in defense projects that directly address capability shortfalls. European countries need to show that their efforts yield results. For that, future projects supported by the European Commission will have to pay off in terms of operational capability and not just help European defense industries win market share. This requires EU projects to be as attractive as possible for member states. If they are too restrictive or bureaucratic, some countries will be tempted to simply go elsewhere for defense collaboration.

The Capability Development Plan (CDP), under the aegis of the European Defense Agency, analyzes member states' defense budgets and procurement plans to identify shortfalls and opportunities for collaboration. It also outlines the priority capabilities that member states have agreed to jointly invest in. The EU's Coordinated Annual Review on Defense (CARD), launched in 2017, has been designed to oversee member states' implementation of the priorities identified in the CDP.

The success of EU-level defense planning will be key to making the EDF a geostrategic program, rather than just an economic policy tool. European countries run the risk of failing to prioritize among capability gaps, potentially misdirecting the EU's money. The European Commission and the European Defense Agency, in cooperation with NATO, are working to clarify how CARD will interact with the latter's defense planning process. Close coordination with NATO is particularly important to ensure complementarity and to assuage fears of institutional competition between it and the EU. It is also crucial because countries that are members of both have already made commitments to fill NATO capability shortfalls—not aligning the two processes would make it much harder to meet both commitments at the same time. This poses particular challenges to smaller European countries with limited resources, forcing them to prioritize.

There is also the question of accountability. Civil society organizations have expressed concern that transferring powers to the European Commission, which is less accountable to voters than national governments, could decrease rather than increase transparency around defense policy, particularly with regard to defense planning and arms exports. The European Parliament should become more involved. When it first voted on the EDF in April, 328 of its members supported the proposal while 231 voted against. Those who are fundamentally opposed to a greater EU role in defense matters aside, lawmakers took issue in particular with the involvement of the defense industry in the drafting of the proposal. They also objected to the European Commission's plans to spend money on disruptive technologies—potentially including artificial intelligence, robotics, and unmanned systems—that some parliamentarians consider problematic from an ethical perspective.

OUTLOOK

In recent years, the European Commission has often acted as a strategic policy entrepreneur, "pushing and pulling" national actors to grant it unprecedented competences in defense. Today, every regulation, every infringement procedure, and every euro in the budget creates the basis for a potential broadening and deepening of the commission's involvement in defense industrial policy. If spending EU money on defense is deemed a success—that is, if it incentivizes member states to spend more and to collaborate more effectively, and if industries see value in working through the EU framework—the budget that will come after the 2021–2027 one might include a larger sum to that end.

However, defense industrial policy remains an overwhelmingly intergovernmental responsibility from the perspective of the EU treaties. The European Commission was able to extend its reach into defense industrial policy because of a surge of political will among member states, and it will need their continued support. Crucial aspects of defense industrial policy, such as arms exports and capability planning, remain largely outside its control.

The European Defense Fund can be considered the "carrot" to the European Commission's (arguably not very effective) defense package "stick." Member states might be more inclined to accept EU money than to follow procurement rules. But, if they deem the conditions to access EDF money as too cumbersome, national players could opt to not bring future big-ticket capability projects, like the next European fighter jet or ground combat vehicle, under the EU umbrella and instead continue to engage in intergovernmental cooperation, try to go it alone, or buy off the shelf from third countries like the United States. And, even if a group of capable countries decides to develop the equipment in question and receives EU funding, the European Commission has yet to develop a plan for how to proceed if member states cannot reach agreement on arms-export rules.

The European Commission's new Directorate General for Defense Industry and Space will be tasked with building an open and competitive European defense market. The challenge will be to maintain a focus on strategic priorities and achieve actual operational outcomes in addition to streamlining the sector. The additional personnel and resources that will come with the new directorate general might help the commission to focus its efforts, including on the EDF, the Action Plan on Military Mobility, and defense-related space policy. It could bundle competences and financial instruments that have been spread out among different directorates general, making the above initiatives easier to navigate for member states, industries, and partners like NATO. Coordination between the new directorate general and the European Defense Agency will have to be worked out. Buy-in from member state governments will prove essential. The commission's ability to take on feedback from industry and advice from military staff at the national and EU levels will be more important than the creation of additional institutional structures. Furthermore, the EU's defense industrial integration can only ever be in service of a common foreign and defense policy. If member states do not agree on interests, threat assessments, and strategy, if they cannot agree on what type of military operations they want to be able to do, even the best supranational EU instruments will remain unused.

Integrating defense industrial policy has the potential to make the EU a more capable defense and foreign policy actor. The European Commission, as a legal regulator with enforcement mechanisms and a budget at its disposal, could play an important role in steering governments and industries. But to prevent defense industrial policy integration happening on paper only, the commission will first have to prove its added value.

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This article is part of Carnegie's project European Defense in a New Transatlantic Context. Support for this research came from the governments of Finland and Sweden.

NOTES

1 As of this writing, the EU's long-term budget still needs to be approved.

2 See Sophia Besch and Beth Oppenheim, "Up in Arms: Warring Over Europe's Arms Export Regime," Centre for European Reform, September 10, 2019, https://cer.eu/publications/archive/policy-brief/2019/arms-warring-over-europes-arms-export-regime.

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