



## Introduction

### 1 Context

Public procurement is the process by which public bodies acquire goods, works and services of civil application. In recent decades, public procurement has undergone what has been described as a “global revolution” in public debate.<sup>1</sup> An important driver of this phenomenon is the significance of public procurement markets for international trade as domestic suppliers increasingly face foreign competition when competing for public contracts. In two of the world’s largest procurement markets, the European Union (EU) and the United States of America (USA), public procurement expenditure accounts for approximately 14 per cent and 10 per cent respectively of Gross Domestic Product.<sup>2</sup> By value, in 2012, these procurement markets were estimated at €1.8 and \$1.7 trillion.<sup>3</sup>

The political, economic and legal significance of public procurement is also reflected in international and regional legal regimes designed to reduce barriers to open public procurement markets. Unlike a national procurement system, the primary objective of which is to obtain value for money for the taxpayer, the principal objectives are to prevent discrimination, enable equal treatment and provide transparency in procurement processes. For example, the World Trade Organization (WTO) provides an option for its members to sign up to a plurilateral Government Procurement Agreement (GPA) providing such guarantees between signatories.<sup>4</sup>

<sup>1</sup> This expression was first used to denote the drivers of change in global public debate identified in S. Arrowsmith and A. Davies (eds), *Public Procurement: Global Revolution* (Amsterdam: Springer Netherlands, 1998).

<sup>2</sup> Estimates based on statistics provided by the Organisation for Economic Cooperation and Development (“OECD”). Available at: <http://stats.oecd.org>. Last accessed 20 September 2015.

<sup>3</sup> L. Cernat and Z. Kutlina-Dimitrova, Chief Economist Note, *International Public Procurement: From Scant Facts to Hard Data*, Directorate General for Trade of the European Commission, 1 April 2015 1, 8–9.

<sup>4</sup> Uruguay Round of Multilateral Trade Negotiations (1986–1994) Agreement on Government Procurement (WTO) (GPA 1994) [1994] OJ L336/273.

The EU has adopted a series of procurement Directives. Regional trade agreements also include chapters on public procurement.

Conversely, whilst many states accord a high priority to the procurement of defence equipment in practice, the legal regulation of defence procurement has only featured peripherally in global debate. Many factors may explain this position. Whilst all forms of procurement raise concerns about the state's need to retain control over budgetary appropriation, the organisation and delivery of public services, and the determination of industrial and social policy, defence procurement is also intimately linked to a core sovereign function, the defence and security of the state. States are inevitably reluctant to open up defence procurement to too much scrutiny or to subject areas of high policy to formalistic procurement rules given the potential to fetter discretion in areas where discretion may be needed most. States also express concern about the ability of procurement rules to safeguard the security of information provided to contractors and the supply of defence material on request, in particular, where contractors are not based in the procuring state. Many states have also used defence procurement to insulate domestic defence industries from foreign competition to maintain levels of domestic employment in the name of industrial policy. Therefore, it is unsurprising that defence procurement has historically been excluded from the GPA and the EU procurement Directives both as a matter of coverage and through treaty derogations permitting states to exempt the full application of open market rules to safeguard their security interests. Limited regulation beyond the national level has, in turn, limited appetite for global legal debate.

However, there may be signs of change. As part of its so-called "Defence Package", in 2009, the EU adopted a Directive coordinating procedures for the award of contracts in the fields of defence and security ("Defence Directive")<sup>5</sup> and a Directive simplifying terms and conditions for the intra-Community transfer of defence-related products ("ICT Directive").<sup>6</sup> Concerning the Defence Directive specifically, the

<sup>5</sup> Directive 2009/81/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of procedures for the award of certain works contracts, supply contracts and service contracts by contracting authorities or entities in the fields of defence and security, and amending Directives 2004/17/EC and 2004/18/EC [2009] OJ L216/76.

<sup>6</sup> Directive 2009/43/EC of the European Parliament and of the Council of 6 May 2009 simplifying terms and conditions of transfers of defence-related products within the Community [2009] OJ L146/1.

aim is to reduce the tendency of many Member States to exempt the award of defence contracts from compliance with procurement rules and EU Treaty principles designed to guarantee non-discrimination. The Defence Directive require national contracting authorities to comply with a set of specially adapted procurement rules modelled on the EU public procurement Directive. The objective is to reduce the high incidence of uncompetitive domestic awards considered partly responsible for the fragmentation of defence markets along national lines and develop a more integrated, competitive EU internal market in the area of defence trade.

The Defence Directive is not only significant from an internal European perspective. For many years, the USA and European countries have argued the need to reduce the USA's significant defence trade advantage on the basis that more balanced reciprocal trade as a result of more open access and non-discriminatory treatment in areas such as defence procurement will improve the overall competitiveness of a transatlantic defence market. This has been considered a necessary step to improve the cost effectiveness and interoperability of defence equipment in the pursuit of effective military and security cooperation. The need for Europe to lead its own initiatives for a more competitive European defence market has also been considered a necessary prerequisite to joint US–European transatlantic initiatives aimed at reducing barriers to transatlantic defence trade. A predominant fear is that, if the USA and Europe enable immediate and unrestricted access to each others' markets now, a less competitive European defence market would be unable to offer the same economies of scale and scope as the US defence market. The result could be an increase in the USA's defence trade advantage, reduce European defence technological industrial capability and threaten even greater dependence on the USA for defence technology and material.

This development may invigorate legal debate not only within the EU but internationally. Firstly, an important issue concerns how the emerging EU legal framework in the field of defence procurement will deal with what may be described as its "external interface". Inevitably, Member States will continue to award defence contracts to contractors from outside the EU ("third countries") and awarded contracts will continue to rely on material sourced from third countries. Secondly, any concerns expressed by the USA or other third countries regarding the potential for the Defence Directive to erect barriers to access and treatment of third country contractors invites consideration of how the USA and other third

country legal and policy regimes governing defence procurement operate in relation to EU and other foreign contractors. Thirdly, both aspects may be considered within the broader context of historical and contemporary initiatives to address barriers to transatlantic trade including the area of defence trade.

*Transatlantic Defence Procurement* offers the first ever consolidated legal analysis of the EU and US defence procurement regulatory regimes. The book is a constitutive exercise intended to provide the framework for future research on at least three key issues. Firstly, the book examines the external dimension of EU law in the field of defence procurement. This is necessary to understand the potential impact of the Defence Directive not only on the internal market but also on international trade. The book examines this aspect with a particular focus on the possible implications for transatlantic defence trade. Secondly, the book examines certain core features of US federal law in the field of defence procurement in light of a comparison of certain features of the Defence Directive. An important objective is to establish a foundation for engaging the US and EU acquisition communities on the legal aspects of defence procurement from a comparative perspective through a “transatlantic defence procurement” discourse. Thirdly, by focusing on defence procurement and its regulation, this book provides the context for a future research agenda examining the impact of other non-tariff barriers on transatlantic and global defence trade from a legal perspective. By opening lines of communication, this book intends to encourage candid and open reflection to the extent possible on a subject that is becoming increasingly difficult to avoid in terms of its impact on regional and global trade. In doing so, the book will serve as an important point of reference for policy makers, legislators, international organisations, procurement practitioners, academics and wider civil society facing an era of increased legal intervention in the area of defence trade.

## 2 Motivations, Aims and Objectives

As indicated, for many years, stakeholders, primarily states and defence industries, have repeatedly sought to exclude defence procurement from the scope of any legal regulation beyond the national level without priority concern regarding access and treatment of foreign contractors in domestic defence markets. Therefore, this book’s focus on the role of defence procurement regulation as a potential barrier to transatlantic defence trade requires careful justification.

### 2.1 *External Dimension of EU Defence Procurement Regulation*

Whilst, as will be discussed, the Defence Directive is not an exclusive motivation for the book; it must be acknowledged that the emerging EU legal framework in the field of defence trade, in particular, in the area of defence procurement, has provided an important catalyst. As this book will discuss, there is now a burgeoning legal literature on the operation of the Defence Directive. Inevitably, legal commentary has first prioritised efforts to understand the scope and substance of the Defence Directive's provisions. Relevant to this book, legal research has already made an important contribution to understanding the potential scope of the Defence Directive's exclusion of contracts implicating third countries under international agreements and organisations. However, the primary focus of legal research has been on the internal operation of the Defence Directive as applied by contracting authorities to contractors within the EU. It is submitted that a focus on what might be termed the "external" dimension of EU defence procurement regulation should be a concurrent priority for a host of reasons.

Firstly, many Member States formerly excluded defence procurement from the scope of EU rules. Therefore, to the limited extent that contracts were not awarded to domestic contractors, certain third countries may have had an equal or even greater stake than contractors from other EU Member States in certain national markets for defence procurement. The requirement to level the playing field for EU contractors but not third countries under the Defence Directive raises corresponding questions about the resulting impact on third country contractors. As will be discussed, the Defence Directive states that Member States retain the power to decide whether or not to permit third country contractors to participate in contract award procedures. It has been identified that the Defence Directive is not, therefore, intended to impact directly on third countries, in particular transatlantic defence trade. However, it must not be overlooked that the Defence Directive, EU law and resulting national laws implementing the Defence Directive may impact third countries indirectly.<sup>7</sup> Secondly, US observers have indicated the possibility for the

<sup>7</sup> M. Trybus, *Buying Defence and Security in Europe: The EU Defence and Security Procurement Directive in Context* (Cambridge: Cambridge University Press, 2014), p. 491: "[...] the relevant trade relations with third countries, especially the USA require attention. Further research is therefore needed, inter alia, on the procurement practice of the Member States on the basis of the Defence Directive and its impact on transatlantic trade."

Defence Directive's provisions to become disguised barriers to market access for US contractors, thereby necessitating analysis of the Defence Directive's application in consideration of third countries. Thirdly, as indicated, the Defence Directive contains several provisions purporting to exclude from its scope contracts awarded in accordance with international agreements involving third countries and the rules of international organisations. Such exclusions may offer flexibility for Member States in the conduct of procurement involving third countries in theory but which have proven to be highly controversial in practice. Fourthly, throughout this period, the EU has been engaged in ongoing efforts to introduce a Regulation on third country access to public procurement and EU access to third country procurement markets. This raises the issue as to whether the EU can, and, if so, how it will address third country relations in the context of defence procurement as a matter of EU law and policy. The Commission has recently indicated its intention to address the "international dimension" of EU defence trade, including apparent obstacles faced by EU industries competing for contracts in third countries, in particular, the USA.

A comprehensive legal analysis of the external dimension of EU public and defence procurement regulation could be the subject of a book in its own right and it is beyond the scope of the book's holistic treatment of defence procurement regulation in the context of transatlantic defence trade. Notwithstanding, this book provides a first preliminary legal analysis. This will offer a framework for future debate on complex unresolved issues such as the respective legal competences of the EU and its Member States to take measures concerning external relations with third countries in the field of defence procurement and the EU's overall regulatory strategy for dealing with third country considerations in application of the Defence Directive.

## *2.2 Legal Aspects of Defence Procurement in Comparative Perspective*

An equally important motivation for this book is the fact that there is relatively limited comparative research on legal aspects of defence procurement. Debate in the field of public procurement is increasingly characterised by debate on whether, and the extent to which, there should be convergence or harmonisation of national, regional and international public procurement law regimes. In turn, this has necessitated growth in comparative legal research on the similarities and differences between regimes with regard to access and treatment of foreign contractors,

including between the US and EU public procurement law regimes. Conversely, the exclusion of defence procurement from regional and international regimes has negated any incentive to examine regulated defence procurement systems in similar terms.

Debate surrounding the Defence Directive has only further exposed the extent to which comparative legal discourse is necessary. US commentary on the Defence Directive has been careful to acknowledge that the Defence Directive is not intended to create a European preference nor specifically facilitate transatlantic defence trade.<sup>8</sup> Notwithstanding, US observers have inevitably identified the potential for certain provisions to become disguised market access barriers, resulting in “discrimination” against US contractors.<sup>9</sup> In order to address those claims, US commentary has tended to reinforce the importance of commitments undertaken in political agreements between the USA and a number of European countries to ensure reciprocal access and treatment in each other’s markets for defence procurement.

Whilst this book examines some of these claims, such claims can often be speculative and difficult to empirically validate in practice. By contrast, a comparative perspective might more constructively draw on the experiences of another jurisdiction to identify how that same jurisdiction deals with similar issues. In turn, this may lead to a better understanding of the nature of the barrier faced and potential ways in which risks of discrimination in the procurement process may be managed or mitigated. Whilst there are encouraging signs in US commentary that US experience may be able to offer important insights for the functioning and development of EU defence procurement regulation, these insights have not been fully communicated or explored. There has also been limited consideration within the USA as to how the US legal and policy framework in the field

<sup>8</sup> J. P. Bialos, C. E. Fisher and S. L. Koehl, *Fortresses and Icebergs: The Evolution of the Transatlantic Defence Market and the Implications for U.S. National Security Policy*, Vol. I, Study Findings and Recommendations (Washington DC: Centre for Transatlantic Relations 2009), pp. 218–19: “[t]he EC Defense Package is not about Transatlantic defense industrial relations or Transatlantic arms sales, and it is not about reorganising or superseding existing U.S. procurement relationships with EU Member States.”

<sup>9</sup> C. Yukins, ‘The European Defence Procurement Directive: An American Perspective’ (2009) Vol. 51 (41) *The Government Contractor* 1: “If the defense directive merely brings new competition and transparency to the European procurement markets, the directive will be a welcome improvement in what was traditionally a closed and uncompetitive market. But if, in practice, the directive is used as an excuse to discriminate against U.S. exporters – or if it is perceived as a tool of discrimination – the directive threatens to trigger serious trade frictions in the transatlantic defense markets.”

of defence procurement is operating with regard to foreign contractors, in particular contractors from the EU.<sup>10</sup> Further, US reaction to the Defence Directive has not prompted similar efforts within the EU to examine the ways in which regulated defence procurement regimes in the USA and other third countries operate with respect to the access and treatment of EU contractors. Yet, as indicated in Section 2.1, the Commission clearly considers access and treatment of EU contractors in third country markets to be an issue meriting investigation. This is perhaps unsurprising given that there have been few attempts within the EU to develop a systematic comparative understanding of the operation of Member States' laws and policies in the field of defence procurement both before and after the Defence Directive, let alone that of third countries.<sup>11</sup>

In light of the above, this book seeks to offer a first comparison of certain key features of the US and EU regulated defence procurement regimes. Critics might argue that the book is just that, a comparison of key features as opposed to a systematic comparative analysis backed by a rigorous comparative methodology. However, by way of an apology, this book is a first in its attempt to juxtapose an emerging regional European coordinating legal framework against a historically highly regulated national defence procurement law regime. A preliminary mapping exercise is of value, in itself in offering an analytically descriptive account of

<sup>10</sup> Many reasons may explain the absence of any historical comparative engagement on legal aspects of defence procurement. Most obviously, prior to the Defence Directive there have been no significant national regimes on which to base any comparison given that defence procurement is lightly regulated in many countries that the USA would class as major defence trading partners. Further, Member States have traditionally excluded defence procurement from the scope of EU rules that have otherwise formed a basis for comparative discussion in the context of public procurement. In addition, the USA has historically relied on limited defence imports and is the world's largest defence exporter. It is perhaps unsurprising that US legal literature has focused more on the negative impacts of its strict legal regime governing defence exports than on issues of foreign access and treatment in US federal defence procurement. The USA may also consider that it is able to respond to the emergence of the EU defence procurement law regime without any significant adjustment to its current legal or policy regime; debate on this issue has not been considered within the USA, however, which arguably further reinforces the need for comparative discourse.

<sup>11</sup> Again, this may be explicable by the fact that historically many Member States have relied extensively on policy strategies rather than the detailed regulation of defence procurement. Further, it is no coincidence that the limited comparisons undertaken in academic research to date have been done in an attempt to make the case for a harmonising EU Directive. See generally, M. Trybus, *European Defence Procurement Law: International and National Procurement Systems as Models for a Liberalised Defence Procurement Market in Europe* (The Hague: Kluwer Law International, 1999). There have been no efforts since.



the US and EU regimes. Beyond description, however, the book identifies important areas of comparison, contrast and interface which provide a framework or context for more systematic comparative research focusing on discrete aspects of the regulated defence procurement process. Further, as this section discusses, the comparative objective is only one of several objectives of this book.

It must also be qualified that the book's objective to encourage greater comparative engagement on the legal aspects of defence procurement should not necessarily be seen as predicated on some naïve conception that it is necessary or desirable for the US and EU defence procurement law regimes to converge under a unified regulated defence procurement system. Rather, the book's objective is to problematise and better understand the impact of legal regimes on market access and treatment of foreign contractors in the EU and US defence procurement markets. However, it is submitted that a better comparative understanding of the operation of regulated defence procurement regimes could also contribute to debate on whether or not convergence would be possible or desirable. Integral to this objective is also the need for the US and EU acquisition communities to use comparative discourse as an opportunity to discuss and exchange best practices, not simply to debate the effects of procurement rules. For instance, legal debate in the field of public procurement increasingly recognises that the harmonisation of legal regimes is unlikely to be effective unless it reflects and is supported by best practices and that there should be greater focus around the harmonisation of best practices rather than harmonisation based around common rules.<sup>12</sup> To this extent, whatever the views on closer convergence or harmonisation of the US and EU regulatory defence procurement regimes, this book encourages the need for the sharing of best practices based on US and EU experience as an important component of comparative discourse. Further, even if defence procurement continues to be excluded from transatlantic and international agreements, comparative perspectives on defence procurement regulation could also offer important insights for debate on the legal regulation of public procurement including its harmonisation.

<sup>12</sup> C. R. Yukins, 'Closing Borders in International Procurement: Next Steps – Part I: Opening Procurement Markets Internationally: An Update on the Road Ahead' (2012) *West Government Contract Year in Review* covering 2011 Int'l 2–1, Int'l 2–6' and D. I. Gordon, 'Anti-Corruption Internationally: Challenges In Procurement Markets Abroad – Part II: The Path Forward for Using Procurement Law to Help with Development and the Fight Against Corruption' (2013) *West Government Contract Year in Review* covering 2012 Int'l 2–10, Int'l 2–18'.

Finally, a transatlantic discourse must be seen as only one comparative perspective. Such a discourse could encourage broader efforts to examine the impact of US and EU regulation outside the context of transatlantic defence trade as well as the examination of regulated defence procurement systems of other major global defence trading nations.

### 2.3 *Legal Barriers to Transatlantic Defence Trade*

A final motivation for the book transcends focus on the emerging EU defence procurement law regime and comparative perspectives on regulated defence procurement regimes. More generally, there is limited research examining the impact of legal regulation as a discrete barrier to transatlantic defence trade. For many years, official publications, (inter)governmental initiatives and academic studies have examined the impact of non-tariff barriers to a more competitive transatlantic defence market in areas such as procurement, export control, foreign direct investment and technical standards, for example. However, the tendency has been to identify the legal frameworks governing these areas as one tangential or peripheral aspect alongside the more substantial impact of policies and practices which collectively create barriers to trade as opposed to assessing the discrete impact of regulation. As will be discussed, there has been some consideration of the impact of national regulatory controls as a barrier to entry to procurement markets in terms of the impact of their costs on the willingness and ability of firms to compete for procurement contracts generally.<sup>13</sup> However, as regional regimes like that under the Defence Directive emerge, there is a basis for focusing more systematically on the distinct role that legal regulation of aspects of defence trade may itself play in erecting barriers to trade not only within the domestic defence markets but also on European, transatlantic and global defence markets. It follows that there has been similarly limited consideration of the ways in which regulatory barriers could be reduced or eliminated or legal instruments adopted in order to contribute towards liberalising transatlantic defence trade.

As indicated, this book focuses on the role of legal regulation as a barrier to transatlantic defence trade as a starting point for a more systematic legal

<sup>13</sup> W. E. Kovacic, 'Regulatory Controls as Barriers to Entry in Government Procurement' (1992) 25:1 *Policy Sciences* 29.