

TOWARDS AN EU BURDEN-SHARING OF DEFENCE COSTS?

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Participants 15th March

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Jean Wesener Secretary General	European Defence Industries Group (EDIG)

Programme for the day:

Session 1

Should EU states contribute to each others' defence budgets?

When Europe's Common Foreign and Security Policy (CFSP) yields EU-backed military responses to a crisis, what will be the budgetary implications? The UK and France stand out as the most capable of mobilising combat forces at short notice, but are unlikely to accept common decision-making on their deployment without some form of compensation.

- If a handful of EU countries are to bear the major part of Europe's future defence burden, is there a case for a new budgetary mechanism that would redistribute military capability costs more evenly?
- What value should be placed on the contribution that defence industries in these countries make to their national economies?

Introductory speakers:

- **Adrian Kendry**, Senior Defence Economist, NATO
- **Sandy Johnston**, First Secretary, UK Permanent Representation to the EU
- **Raphaël Mathieu**, Researcher, Royal Defence College

Session 2

The economic benefits of enhanced defence cooperation

The beneficiaries of a better-functioning European market for defence equipment, and from EU programs like Star 21, are likely to be those with well-established defence industries. Is enhanced European defence cooperation a reality and if so, what examples point to the future?

- Can the economic stimulus of defence technologies be measured as a way of encouraging EU states to work together more closely?
- What are the business opportunities for SMEs and what is the job creation potential of defence work?

Introductory speakers:

- **Martin Hill**, Vice President, DefenceThales
- **Vicente Martinez Candela**, Defence Counsellor for Armaments and NADREP, Delegation of Spain to NATO

Key points of the debates

At its latest roundtable, the New Defence Agenda discussed how defence costs could be shared across the EU. However, as the day progressed, there was a gradual change of topic with the focus moving firmly to security. Moderator **Michel Berendt** opened the morning session by noting that it was difficult to separate defence and security and later, Thales' **Martin Hill** observed that industry was mainly talking security, as it was "chasing the money".

Several speakers emphasised the gap in expenditure between Europe and the US and there was universal acceptance that defence budgets were being squeezed. Europe therefore needed to get more bang for its euros – not forgetting the odd pound or two. Another recurring theme was the need to harmonise defence requirements, as NATO's **Vicente Martinez Candela** noted that a pre-requisite for creating common budgets was an agreement on common policies.

Throughout the discussions, the main stumbling block towards enhanced co-operation and burden-sharing was not difficult to identify: NATO's **Adrian Kendry** said that the EU was "operating in a sea of nation states" while UKRep's **Sandy Johnston** stressed while the EU would continue to decide collectively on the launching and running of military and civilian operations, member states would be unlikely to relinquish national decision-making over the deployment of their armed forces. This need for political agreement within the EU was taken up by Candela, who identified it as the solution to reduce the barriers protecting EU's fragmentation. Johnston made a similar point, saying that progress would be even more difficult in an EU of 25, "where everyone has an equal voice".

However, this was one debate where the man in the street was not ignored. Kendry commented that we should do a better job in explaining to the public the nature of different threats that are faced. Johnston was one of several speakers to note that "spending more on defence" was not a vote winner. Going further, he raised concerns about the problems caused by the views of the media in the UK, and how it could influence policy. Certainly, recent events in Madrid have shown the power of the public and it will be increasingly difficult for member states to relinquish national sovereignty whenever defence or security issues are raised.

As for industry, both Candela and Johnston stressed the need for improvements in that sector. This brought EDIG's **Jean Wesener** (almost) to his feet. He made a spirited defence of the defence industry, commenting that "Europe needs to reorganise itself more than industry" and adding that EDIG had been begging for harmonised requirements for 20 years.

On a practical note, the Royal Netherlands Military Academy's **Rob de Wijk** stressed that national efforts at cooperation had been pushed to their limits and it was essential to start making supranational decisions. Although he acknowledged the difficulty in achieving this in an enlarged EU, de Wijk recommended the creation of a "common procurement budget" as a first step.

With cries of "show us the money" echoing around the table, it was left to the late arrival of the European Commission's **Tjien-Khoen Liem** to raise the meetings' spirits. Introducing the Commission's report *Research for a Secure Europe*¹, that had been presented to Commission President Romano Prodi that morning, Liem declared that it recommended funding of 1 billion euros per annum on security research. He added that this would complement national spending and any expenditure authorised by the Agency. That body was seen by some as a possible vehicle for coordinated actions but others had their doubts.

Although there was general acceptance that good progress had been made on the ESDP, Berendt closed the meeting on a pragmatic note, saying that great leaps forward may not be possible in an enlarged EU of 25 member states without an agreed constitution."

¹ http://europa.eu.int/comm/research/security/index_en.html

Session 1: Should EU states contribute to each other's defence budgets?

Referring to the recent terrorist attacks in Madrid, Government Policy Consultants International's **Michel Berendt**, the day's moderator, said that defence and security issues were now part of a broad package and were difficult to separate. Given this situation, Berendt noted that the topics of the morning and the afternoon could well overlap.

First speaker: Adrian Kendry, Senior Defence Economist, NATO

Speaking personally, **Adrian Kendry** agreed that the Madrid bombings would impact discussions in regard to the appropriate sharing of security and defence costs. But Kendry reminded the session that countries such as the UK and Germany were under pressure to reduce defence spending and it was now a question of what was affordable. Casting doubt as to whether the EU states were willing to co-operate on defence matters, Kendry argued that the EU was operating in a "sea of nation states".

Examining what Europe was spending on defence in comparison to the US, Kendry noted that even though Europe's GDP was 75% of the US's, its defence budget was only 46% of its transatlantic cousin. As for what Europe got for its money, Kendry argued that it only achieved 25% of the US's capabilities for a similar outlay.

With that background, Kendry acknowledged that sharing costs could help the EU to achieve a better return for its money. However, he was unsure if satisfactory mechanisms existed to allow equitable sharing. From a practical viewpoint, Kendry noted that sharing costs within a nation state was difficult enough, never mind across countries. He also argued that the situation would become more complex due to a) EU enlargement and b) the difficulty in separating homeland security and defence issues.

Second speaker: Sandy Johnston, UK Permanent Representation to the EU

Also speaking in a personal capacity, **Sandy Johnston** opened his remarks by noting that the UK and France remained joint first among equals in terms of individual EU nations' defence capabilities. Putting this down to largely historical reasons, Johnston then set definite limits on any envisaged "collective decision making". EU Ministers already took collective decisions to launch military actions but the issue of participation and the deployment of national assets remained one for Member States acting individually. Any suggestion that other Member States might share the burden of those who were more capable by actually contributing to the cost of their forces was likely to lead to a desire on the part of all such contributors to have a say in when those forces were deployed. This was unlikely to be acceptable to national governments. His preferred solution was for those other member states to spend more on defence. However, as he acknowledged that this was an unlikely scenario – Johnston argued, like Kendry, for more effective defence spending.

Putting forward a case for smaller professional armed forces and more mobile capabilities to be the order of the day, Johnston said that work was proceeding within the EU on Headline Goal 2010. This had a particular focus on qualitative improvements and the so-called "ilities" – deployability, sustainability, interoperability, capability, flexibility, etc. as well as the battle group concept. And returning to a familiar theme, Johnston made a case for harmonising requirements and standards, and collaborating on standards and procurement. The nascent European Defence Agency would have an important role to play here.

Johnston did not ignore the defence industry in his review of the situation, but added a word of warning. He said it had an important role to play if it: a) adapted and remained competitive

and b) did not seek to play a part in introducing a “fortress Europe” – Europeans must be free to buy from wherever they could get best effectiveness and value for money.

Third speaker: Raphaël Mathieu, Researcher, Royal Defence College

The Royal Defence College’s **Raphaël Mathieu** presented a summary of a complex study - *Convergence criteria in the field of defence: budgetary aspects* - that looked at comparative defence spending in EU member states since 1990. Mathieu gave an overview of the study’s results in comparing operational criteria and threat criteria, but focused most of his attention on economic criteria.

Mathieu’s results on comparing economic criteria indicated that although member states agreed on the need to increase expenditure, it was difficult to agree on a binding process, e.g. that a certain percentage of GDP should be spent. The results showed a decrease in the mean expenditures over the period of the study (graphics 1 & 2). Actual expenditure was usually greater than the budgeted amount (between 1990 and 2001) and the UK was well positioned in terms of military spending per capita (graphics 3 & 4). However, over the eight year period, actual military expenditures appeared to have increased in many countries (graphics 3 & 4). Mathieu explained that this was due to personnel cuts going faster than the budget decreases.

The graphical results of the study are shown in the appendix (partly in French).

First session – Q&A

Summing up the remarks from the first session’s speakers, Berendt noticed that while everyone agreed on the need to increase spending on defence, there was a general trend towards decreasing actual expenditures. This meant that money had to be spent more efficiently.

Throwing open the session for questions from the floor, the first intervention came from Defense News’s **Brooks Tigner**, who wanted to know what was actually holding expenditure back given that there was agreement that spending on defence and security should increase.

In response, **Sandy Johnston** said that while initiatives were underway to try to focus expenditure more effectively, there was little prospect of member states releasing sovereign authority over their own budgets, where defence expenditure had to compete with other government priorities such as housing, health spending and education. Defence Ministers and Foreign Minister would indeed like to see more defence spending, but sadly they did not run their Finance Ministries. Emphasising the seriousness of the situation, Johnston underlined the voluntary, bottom-up nature of capability development in the EU - not like NATO (with its top-down management style), in that there were 25 member states and they all had an equal voice.

Furthermore, Johnston insisted that progress to date on the ESDP had been remarkable, but that it was impossible to go faster than individual member states allowed. Relaxing the tone for a moment, Johnston jokingly added that even the UK’s policy was sometimes influenced driven by the views of the Daily Telegraph and the Daily Mail. Certainly, he added, politicians had to pay attention to such strident and popular voices.

Adrian Kendry then explained how NATO was addressing a whole range of issues, many of which would be discussed at the forthcoming Istanbul Summit. As for moving forward, Kendry referred to an ongoing major debate that covered subjects such as the release of sovereignty and how to move towards joint training initiatives and shared procurement - the aim being to achieve better overall capabilities.

Kendry explained that the Alliance was going through a significant set of discussions prior to Istanbul; topics included how the new members could be integrated into NATO (perhaps by focusing on their niche capabilities), how the Mediterranean Dialogue States² might impact the Alliance if they gained full membership, etc.

Kendry also discussed the situation faced by NATO as it was operating on the borders of Pakistan, India and China due to its presence in Afghanistan. He outlined a complex picture to explain why NATO was being held back, despite its vision of a “common armament approach” that linked homeland security and defence expenditure.

At this stage, the NDA’s Director **Giles Merritt** intervened to pose two supplementary questions:

- a) what would happen to member states that did not have sophisticated military capability if, as appeared likely, countries such as the UK and France did not allow others to buy-in to their sovereign military capacities?
- b) as new EU member states were not under serious pressure to increase their defence expenditures, the US was retaining its involvement in Bosnia even though an EU force is due to take over there later this year from NATO’s SFOR. What incentives would enable the EU to break the burden-sharing deadlock so the US will consider them as “grown-us”?

Kendry argued that there was still a problem between buying-in to capabilities and the subsequent problems that may cause in decision-making. As for the EU being under pressure to invest in better capabilities, he argued that it was facing demands from the defence manufacturing and research community that wanted better military investment (more coordination and cooperation, more efficient use of funds, etc.). But he underlined, yet again, the need to clarify what exactly Europe should be doing and what the electorate wants Europe to do with its capabilities. Kendry added that there was a need to explain the whole range of threats to the electorate, as they cover much more than just terrorist attacks.

His final comment was a call to clarify the sharing of tasks and capabilities (law enforcement, intelligence, military actions, etc.) between the EU and NATO, as without that no one could say if the EU was mature enough to replace NATO in Bosnia (S4).

Johnston added several pertinent points:

- a) member states look towards the UK and France (as “experts in warfare in the 21st century”), but they should be encouraged to contribute more to the EU’s overall capabilities. “We do it well but we cannot afford to do it for the whole of the EU”.
- b) there is no willingness at Government level to spend more as this “does not win votes”, neither is it a priority in comparison with education, housing, social services, etc.
- c) ESDP aimed to harness a European dynamic and to persuade Member States to do for the EU what they had consistently failed to do in NATO, which some may see as a US-dominated club. Johnston suggested that if the EU performed well in promoting peace and stability, for example in Bosnia, or in combating terrorism it might help the argument to spend more. However he dismissed the idea that a residual NATO presence in Bosnia would be “keeping an eye on the EU” (particularly given the relative sizes of the forces) and insisted that the US was simply better placed in some areas, e.g. intelligence gathering, because of its experience in the region.

His final point was that nothing would work unless the political will existed. Johnston hoped that the EU would be allowed to work in a genuine strategic partnership with NATO; for

² The countries taking part in NATO’s Mediterranean dialogue are Jordan, Algeria, Egypt, Israel, Mauritania, Morocco and Tunisia.

example, the battle groups concept should complement the NATO Rapid Response Force. The EU should be made to work coherently across the board, deploying its broad range of capabilities, including policing. There should be no competition with NATO – it should be a question of synergy and complementarity.

With Berendt making a further call for questions from the floor, EDIG's **Jean Wesener** took the opportunity to respond to Johnston's earlier comments about the defence industry. Wesener agreed that industry must face up to its responsibilities but reminded the audience that EDIG had been "begging for a harmonised set of requirements and for common procurement for 20 years". He added that governmental projects should be seen through to the end and that original schedules should be respected. Speaking passionately, Wesener reasoned that Europe needed to reorganise itself more than industry.

Responding to Johnston's comment that Fortress Europe should be avoided, Wesener said it would happen anyway given the current rate of European companies being acquired by US interests. He added that design capability would move to the US, European governments would no longer have the freedom to decide on which operations should be undertaken and US industry would be favoured over its European counterparts.

The Royal Netherlands Military Academy **Rob de Wijk** brought the discussion back to the deadlock over burden sharing. He argued that sharing of common costs was not the solution as we had "reached the limits" of international cooperation. De Wijk therefore called for bold actions to be taken, by way of introducing supranational decision-making in the realms of defence. He acknowledged that this would be extremely difficult and that the complexity would only increase after enlargement.

However, de Wijk did see a few white clouds on the horizon as the draft Constitution did discuss permanent structures for cooperation, with elements of supranational decision-making and it did discuss battle groups within the EU.

But he did call for more practical steps, as most member states are focusing on the transformation of their armed forces, (i.e. new doctrines, new technology, network centric warfare, etc.) De Wijk quoted calculations that showed a minimum of 30% of the EU's defence budgets was needed to achieve necessary modernisation and transformation. His answer was to create a common procurement budget as a first step, that might be 5% of the collective defence budgets to be spent on transition and transformation (such as strategic lift, NBC protection, etc.).

Berendt suggested that such broad political initiatives might not be forthcoming after the failure of the Convention and wondered if progress might best be made by many small steps or a "huge program to change the nature of expenditure". **Raphaël Mathieu** closed the session by suggesting that budgets be examined so that focus is placed on R&D and acquisitions, as sometimes purchases were made when equipment was not required. He also called on member states to look not so much to their own interests as to Europe's.

Session 2: The economic benefits of enhanced defence cooperation

First speaker: Martin Hill, Vice President, Defence Thales

Martin Hill focused his remarks on the benefits of cooperation and insisted that industry-to-industry cooperation was already a reality. Using Thales as an example, he explained that it had a British company in the UK, a German company in Germany, a Norwegian company in Norway, etc. Adding that other companies (EADS, BAE Systems, AMS) had parallel strategies, he outlined the benefits for industry: shared risks, shared budgets for R&D, longer production lines through cooperative production, shared production of services, etc.

Hill reasoned that while industry was successfully cooperating, nations were not allowing other nations to interfere in their defence interests, i.e. there was a total lack of inter-nation cooperation. On the positive side, Hill gave examples of public / private partnerships that were working, e.g. in air-to-air refuelling, sea-lift, strategic airlift, logistic support and training, etc. Describing these initiatives as “successful and cost effective”, Hill reasoned that this trend would continue.

Looking to the future, Hill stated that cooperation was the key in order to utilise research funds effectively and achieve economies of scale in production. However, Hill had a warning. He explained that Thales was involved in discussions with representatives of several military forces, in regard to equipping the soldiers of tomorrow. What was needed was “some form of cohesion between the programmes”, in order to avoid reinventing the wheel.

This took Hill to the subject of the Agency, which could resolve these issues. He argued that although the processes (Helsinki Goals, ECAP and establishing the necessary project teams) exist today, future efforts must be based on a wider European basis to allow for the necessary operational flexibility and reduced costs.

Hill stated that the Agency needed to look at: delivering military capabilities, supporting defence and security R&T, launching new European programmes and promoting a sound EDEM³ and DTIB.

A trickier subject in his opinion was security. Hill argued that elected governments played down defence, which led to complacency. Hill said it took an event like 9/11 to make things happen and now defence and security were becoming increasingly blurred.

Hill commented that security had not had the investment and large programmes that defence had enjoyed, as there were many customers in the security field (government offices, police forces and private companies), i.e. it was a fragmented market. On the other hand, the defence industry was used to dealing with large single customers. Hill therefore called for the security industry to change, and argued that the large high-tech defence companies could be a likely vehicle for that change.

Hill concluded that consolidation had already started to create the EDEM and that more cooperative programmes would enhance this. He foresaw security expenditure increasing, with more jobs being created, and stated that the Agency would be a vital vehicle to foment this change.

³ European Defence Equipment Market

Second speaker: Vicente Martinez Candela, Defence Counsellor for Armaments and NADREP, Spain's Delegation to NATO

Vicente Martinez Candela opened his remarks by stating that the European Defence Market was only a dream, as "Europe has national markets ruled by national policies". Martinez Candela therefore used his remarks as an opportunity to outline how this problem could be overcome. He explained that the first challenge was to see how the Framework Agreement (LOI) could be extended to all member states and seen in the context of the EU as a whole.

Turning to R&D, Martinez Candela said that the concept of shared funding of common research was a difficult one to be accepted as it meant part of the scarce national R&D resource money could go to the promotion of foreign industries.

Welcoming the decision to create the Agency, he nevertheless said that progress would take time and be difficult. The first problem for the Agency would be the issue of fragmentation, both on the demand and production sides. Then, given the necessary legal and political support, he added that the Agency would be able to start multinational programmes from coordinated capabilities and not from national technical solutions, as was the case today.

Also looking at the need for cooperative R&T, Martinez Candela stated that existing initiatives of the Framework Agreement for Defence Industry Restructuring, the EUROPA MOU and the WEAO Research Cell would provide the Agency with a valid initial basis to operate in this field. He stressed the need to pay attention to dual-use technologies, which require close coordination between the Agency and the European Commission as well as the assignment of necessary EU funding.

In conclusion, Martinez Candela looked at the STAR 21 report recommendations that called for a ".....a European armaments policy to provide structure for European defence and security equipment markets, and to allow a sustainable and competitive technological and industrial base....." He noted that preliminary discussions had started and that the development of the necessary EU Armaments Policy would gather pace with future implementation and operation of the Agency.

As a final point, Martinez Candela reasoned that enhanced co-operation would produce favourable conditions not only for European prime-contractors but also for the essential development of SMEs for which the EU must create the necessary infrastructure and financial support was developed. He added that Defence industry must improve its own efficiency and be able to produce and efficiently tailor the same product for different customers.

Second session – Q&A

EDIG's **Jean Wesener** felt obliged to once more defend the role of industry and repeated his call for a) harmonised requirements to avoid fragmentation and b) movement towards common procurement and economies of scale.

Stating a personal wish, Wesener called for an agency backed by centralised funds, commensurate with the disbanding of the 25 national agencies – suggesting this could be the start of a common defence policy for Europe.

Michel Berendt referred to the presentation of a policy document, on research into security, to European Commission President Prodi that very day and asked **Martin Hill** for his thoughts on how public-private partnerships could be moved forward.

Hill highlighted the EU's problem in distinguishing between defence and security. He reasoned that in the area of dual-use technology, most companies involved would be from the defence industry. Hill therefore asked if the security industry need assistance from the defence companies if a sizeable budget was forthcoming from the Commission.

Vicente Martinez Candela reminded the meeting that the EU had not yet reached any common conclusions about common defence and that security was a very unknown field indeed. He also warned the meeting that much of security research was confidential as otherwise it could easily be used against the originators. Expressing a personal view, he said that it was common sense to expect that common budgets would follow common policies and meanwhile multinational cooperation and coordination would be the way forward.

Wesener gave his view of the difference between defence and security with reference to events in Iraq; he said that the US had demonstrated a powerful form of *defence* that had led to the need for *security* throughout the country. He added that another difference was that ministries of defence placed defence contracts whereas ministries of internal affairs were responsible for security – “it was a different kettle of fish”. In conclusion, Wesener said that the European institutions might not be able to deal with defence (could not spend money) but they could make recommendations in the field of security.

Giles Merritt intervened by bemoaning the fact that defence was always seen as a cost, i.e. that its advantages were often ignored. He also called for the UK and French defence industries to make more efforts to explain the tangible benefits they make to their national economies. Moving on to the Agency, Merritt suggested it could be used to act as catalyst to transform European capabilities.

The IABG's **Uwe Nerlich** disagreed with Wesener's definition of defence, as it was “too narrow”; Europe was at the beginning of a transformation process. He cast some doubts on the ability of the Agency to solve all the issues as it would have a small staff and would look at capability development (possibly including research) and not be responsible for common procurement. Nerlich reasoned the Agency would need extra funds and called for people to think creatively in this regard.

The European Commission's **Tjien-Khoen Liem** arrived to give an overview of the European Commission's paper – “*Research for a Secure Europe*”. He explained that it covered intra- and extra-territorial missions as well as civilian missions perhaps accompanied by military measures. Liem declared that one of the main recommendations was the creation of a European security research programme with an annual budget of approximately 1 billion euros, from 2007. He argued it could be an anchor point for technology development in support of security.

As for definitions about the meaning of security and about the difference between civil and military operations, Liem commented that no clear lines could be drawn and that such definitions were not useful in research terms. He preferred that every euro spent on research was beneficial for European citizens and society.

Liem said that this would not be the only pot of money linked to security research and added that the Agency could also play a part in supporting security research. He also said the European funding would complement national programmes, which should continue.

Closing remarks from the panel

Vicente Martinez Candela reminded the audience that to progress Defence cooperation in the EU, political agreement was needed to overcome national barriers. In regard to the European Commission's R&T proposal, he offered an opinion that the Commission and the Agency must work together mainly for the areas of dual use technology and technologies overlapping defence and security, but insisted that working EY structures were needed to achieve practical cooperation in both fields – including collaboration with the US.

Noting that the meeting had spent most of the time focussing on security rather than defence, **Martin Hill** said that this illustrated that industry was once again “chasing the money” and that, as pointed out by Liem, there was little difference between the two domains. He also asked for clarification on the identity of the new customer, as the ministries of the interior were

not used to dealing with big procurements contracts, i.e. “transformation is needed on the industrial side”.

From the floor, **Tjien-Khoen Liem** agreed with Hill but noted that expenditure on security was a long-term project, which needed harmonised long-term requirements and less fragmentation. For Liem, standardisation and communication were the way towards coordinated research ... “in a decade or so”.

In respect to the Commission Initiative on Security R&D, Martinez Candela saw two potential and critical problems that require previous political agreement; how would strategic Security technologies be selected at the European level and how would the use of those European technologies be controlled?

Michel Berendt took those questions as an indication as to how far the EU had progressed in discussing the wider aspects of security and defence. He concluded the meeting by noting that as it was difficult to distinguish between security and defence, the European institutions must find a way forward even though there was no fixed Constitution and there would soon be an EU of 25 nations.

Next meetings

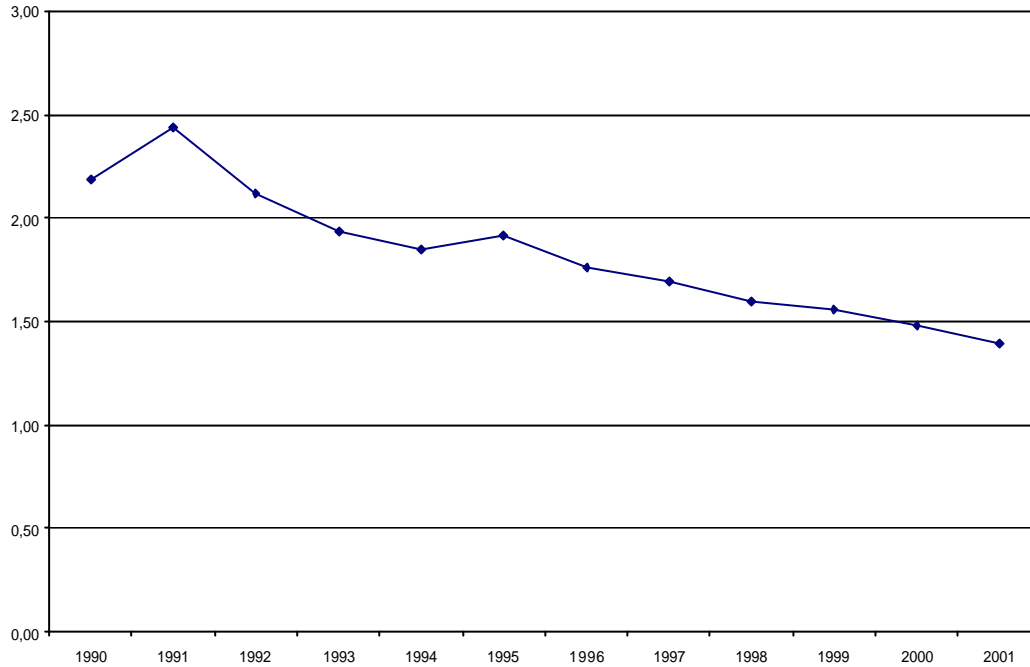
The next roundtable will be held on April 26 – **Assessing the military threats of the future**

The NDA’s annual security and defence conference in Brussels will take place on May 17th – **Defending Global Security : The New Politics of Transatlantic Defence Co-Operation**

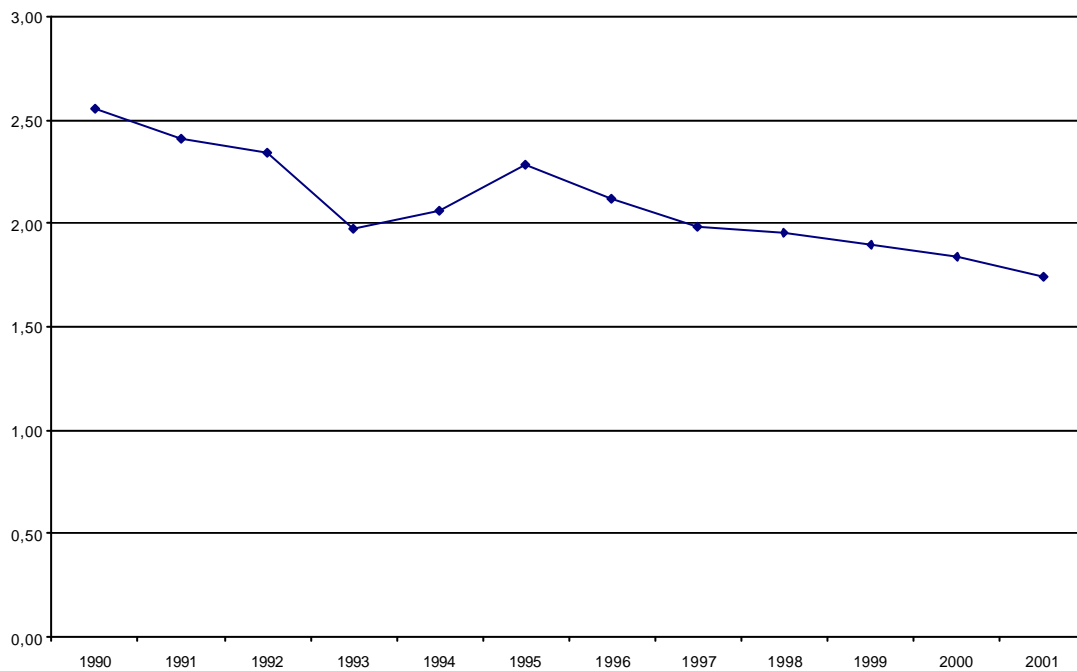


Appendix⁴

Evolution of military budget: The EU fifteen (in percent of GDP)

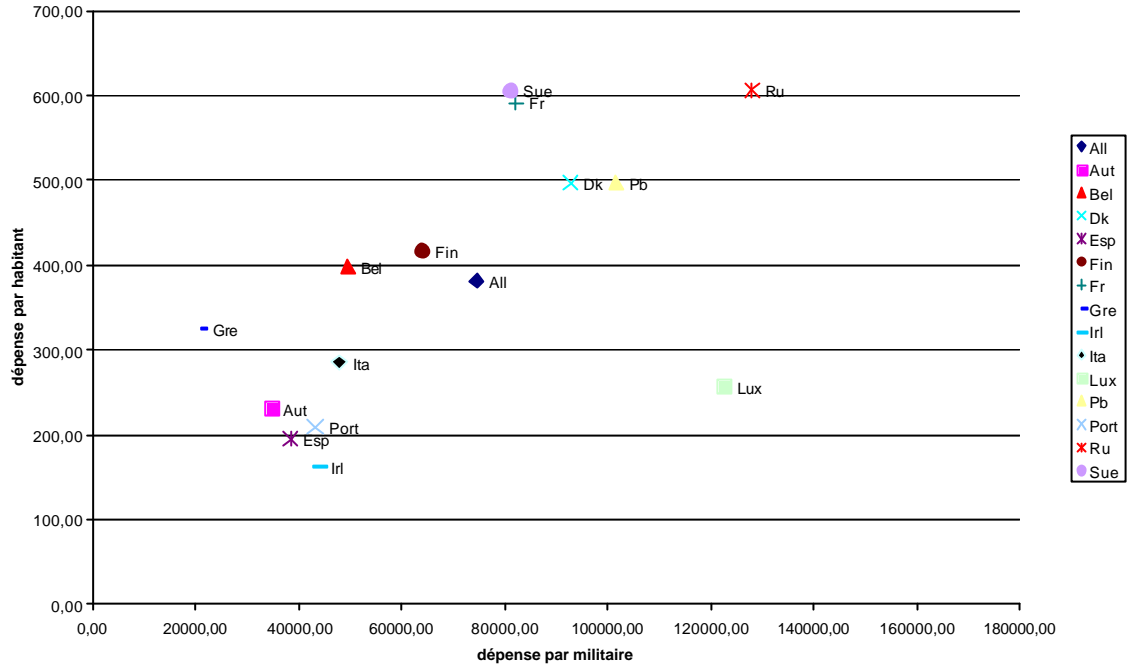


Evolution of defence spending: The EU fifteen (in percent of GDP)



⁴ Distributed by Mr. Mathieu during the March 15 Roundtable. Taken from the CDS study « *Convergence criteria in the field of defence: budgetary aspects* », released in November 2003 and available shortly (in French) on the Royal Defence College website.

Defence spending by habitant and by military in 1993



Defence spending by habitant and by military in 2001

