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COVER NOTE

From: Secretary-General of the European Commission, signed by Ms Martine DEPREZ, Director

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To: Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union

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Subject: COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT pursuant to Article 294(6) of the Treaty on the Functioning of the European Union concerning the position of the Council on the adoption of a Regulation of the European Parliament and of the Council establishing the European Defence Fund

Delegations will find attached document COM(2021) 143 final.

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TO THE EUROPEAN PARLIAMENT**

pursuant to Article 294(6) of the Treaty on the Functioning of the European Union

concerning the

**position of the Council on the adoption of a Regulation of the European Parliament and
of the Council establishing the European Defence Fund**

(Text with EEA relevance)

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of the Council establishing the European Defence Fund**

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1. BACKGROUND

Date of transmission of the proposal to the European Parliament and to the Council (document COM(2018) 476 final – 2018/0254 COD):	13 June 2018
Date of Council partial general approach:	19 November 2018
Date of trilogue 1:	16 January 2019
Date of trilogue 2:	5 February 2019
Date of trilogue 3:	19 February 2019
Date of the progress report reflecting the common understanding reached at the third trilogue in the Committee of Permanent Representatives:	27 February 2019.
Date of the position of the European Parliament, first reading:	18 April 2019.
Date of Council agreement on a revised negotiation mandate:	30 September 2020
Date of trilogue 4:	30 November 2020
Date of trilogue 5 (final):	14 December 2020
Date of political agreement in the Committee of Permanent Representatives:	18 December 2020
Date of the ITRE Committee of the European Parliament voted to endorse the compromise agreement:	14 January 2021
Date of adoption of the Council first reading position:	16 March 2021

2. OBJECTIVE OF THE PROPOSAL FROM THE COMMISSION

The European Union (EU)'s geopolitical context has changed dramatically in the last decade. The situation, globally and in its neighbouring regions, is unstable and it faces a complex and challenging environment in which new threats, such as cyber-attacks and other hybrid threats are emerging, whilst more conventional challenges are also returning.

European defence, and the European defence industry face significant market inefficiencies, linked to untapped economies of scale (fragmentation of national markets with a single buyer) and resources overlaps at national level. The demand comes almost exclusively from Member States, but their defence budgets, in particular for research and development (R&D), have seen important budget cuts in the past 10 years. The sector is largely fragmented across national borders, with substantial duplications and resulting inefficiencies in terms of failure to capture economies of scale and learning. Despite the combination of increasing costs and stagnating or shrinking defence budgets, planning, R&D spending and the procurement and maintenance of equipment have remained largely matters for individual Member States, with very limited cooperation between them. This lack of cooperation between Member States further weakens the ability of the EU defence industry to sustain the industrial and technological capabilities necessary to preserve the EU's strategic autonomy and meet its current and future defence and security needs.

The European Defence Fund is intended as an instrument to foster the competitiveness and innovativeness of the European defence technological and industrial base, thereby contributing to the EU's strategic autonomy. It aims to trigger cooperative programmes that would not happen without an EU contribution and, by supporting research and development activities, to provide the necessary incentives to boost cooperation at each stage of the industrial cycle.

Collaborative projects with significant cross-border participation by small and medium-sized enterprises will be particularly encouraged. This will ensure that the Fund remains open to participants from all Member States, based on their ability to contribute to its objectives and regardless of their size and location in the Union.

3. COMMENTS ON THE POSITION OF THE COUNCIL

The Council's position reflects the agreement reached in the trilogues. The most important changes introduced compared to the Commission's proposal include:

- *Budget:* The financial envelope for the implementation of the Programme for the period 2021-2027 shall be EUR 7 953 000 000 in current prices. The distribution ratio of the amount has been kept at one third for research actions and two thirds for development actions.
- *Duration:* Alignment of the European Defence Fund to the duration of the MFF 2021-2027.
- *Governance:* EDF annual work programmes and award decisions for both research and development actions shall be adopted in the form of implementing acts (double comitology) with use of the examination procedure, whereby the draft implementing act may not be adopted where no opinion is delivered. The Fund shall be implemented in direct management, but by way of derogation in justified cases specific actions may be implemented under indirect management by bodies referred to in Article 62(1)(c) of the Financial Regulation; such derogation however shall not cover the selection and award procedure.

- *Eligible actions:* Actions for the development of lethal autonomous weapons without the possibility for meaningful human control over selection and engagement decisions when carrying out strikes against humans shall not be eligible for support from the Fund, without prejudice to the possibility of providing funding for actions for the development of early warning systems and countermeasures for defensive purposes.
- *Disruptive Technologies:* At least 4% and up to 8% of the financial envelope shall be allocated to calls for proposals or awards of funding supporting disruptive technologies for defence, thus marking an increase of the 5% ceiling initially proposed by the European Commission.
- *Ownership of results:* Exclusion of results that are subject to control or restrictions by a non-associated third country or non-associated third country entity and ex-ante notification to the Commission shall be obligatory, thus limiting the margin of discretion of the Commission in applying these conditions on a case-by-case basis. Clarification that the EDF regulation shall not affect the discretion of Member States as regards policy on the export of defence-related products. Addition that Member States or associated countries shall have access rights to results of research actions on a royalty-free basis that are necessary for the execution of joint follow-up activities.
- *Consultation of the project manager:* Replacement of an information requirement initially proposed by the European Commission with a consultation requirement.
- *Rules on classified information:* Introduction of a possibility for Member States to decide on a specific (national or intergovernmental) security framework for the protection and handling of classified information relating to the action.
- *Ethics:* Actions implemented under the Fund shall comply with the relevant national, Union and international law, as well as with ethical principles reflected also in relevant national, Union and international law, including in particular international human rights and international humanitarian law. To facilitate the compromise the Commission declared that it intends to provide guidance on ethics in defence-related research and development to applicants, as well as to independent experts tasked with ethics screenings and assessments of proposals.
- *Coverage of indirect costs:* Indirect costs can be determined by two alternative ways to be chosen by the beneficiaries (25% flat rate or a determination based on actual indirect costs). To facilitate the compromise the Commission declared that it will respect the principle of sound financial management (and thus principles of economy, efficiency and effectiveness) as embedded in the Financial Regulation.
- *Cumulative, complementary and combined funding:* Deletion of the horizontal provision initially proposed by the European Commission as shared management funds such as structural funds are typically geared towards projects with a single beneficiary from a single Member State.
- *Resources allocated to Member States under shared management:* Co-legislators could not agree on the possibility to transfer shared management funds to the European Defence Fund. To reach a final compromise the respective paragraph was deleted.
- *Protection of the financial interests of the Union:* Addition of a recital with a reference to the general regime of conditionality for the protection of the Union budget against breaches of the principles of the rule of law.

- *Climate*: Update of the reference to the overall climate-spending target for the entire MFF (initially 25%) to 30%.
- *Cybersecurity*: Deletion of the reference to the European Cybersecurity Industrial, Technology and Research Competence Centre, reference to the Joint Communication on cybersecurity was maintained.

The Commission considers that the agreement reached preserves the objectives of the Commission's original proposal.

4. CONCLUSION

The Commission accepts the position taken by the Council.